Supreme Court, U.S.
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No. 03-1034

In the Supreme Court of the United States

ESTATE OF BURTON W. KANTER, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

The Tax Court keeps secret, even from the reviewing courts of appeals, the findings of fact and credibility judgments of its special trial judges. By law, these trial judges are required to file reports containing findings of fact and opinion with the Tax Court. Tax Ct. R. 183(b). By law, these findings of fact "shall be presumed to be correct" and the Tax Court is required to give "due regard" to the circumstance that the trial judge "had the opportunity to evaluate the credibility of witnesses." Tax Ct. R. 183(c). Nonetheless, the Tax Court overturns the factual findings, including the credibility findings, of its trial judges without the record revealing those findings or that the Tax Court has overturned them. Secret trial judge reports preclude the courts of appeals from determining whether the Tax Court has complied with the legal constraints described above. Secret trial judge reports also preclude the courts of appeals from reviewing a Tax Court decision on the basis of the entire record on which that decision in fact rests. Federal statutes require that "all reports of the Tax Court * * * shall be public records." 26 U.S.C. § 7461(a). The questions presented are:

1. Whether the due process clause or the governing federal statutes require that the courts of appeals be able to review Tax Court decisions on the basis of the complete record, including the trial judge's findings of fact that, by law, the Tax Court must presume to be correct.

2. Whether Tax Court Rule 183 requires judges of the Tax Court to uphold findings of fact and credibility judgments made by their trial judges unless those findings are "clearly erroneous," as the D.C. Circuit has held, or are those findings and credibility judgments entitled to no deference at all, as the Seventh Circuit held in this case.

RULE 14.1(b) STATEMENT

The following are the parties to the proceeding in the Court of Appeals for the Seventh Circuit:

1. Estate of Burton W. Kanter, Deceased
2. Joshua S. Kanter
3. Naomi Kanter

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OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a to 97a) is reported at 337 F.3d 833 (7th Cir. 2003). The opinion of the Tax Court (App. 98a) is reported at 78 T.C.M. (CCH) 951 (1999). The orders of the United States Tax Court (App. 99a-112a) denying access to the Special Trial Judge's Rule 183 Report are unreported.

JURISDICTION

The judgment of the court of appeals was entered on July 24, 2003. A timely petition for rehearing was denied on October 21, 2003. App. 115a. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISION, STATUTES AND RULES INVOLVED

Relevant constitutional provisions, statutes, and rules are set forth at App. 116a to 121a.

INTRODUCTION

The question presented here concerns the constitutionality of procedures now routinely used by the Tax Court to impose massive liability, including judgments of tax fraud, in the most serious class of tax cases it assigns its special trial judges. In upholding the Tax Court, the divided court below endorsed a procedure, unheard of in American law, in which the Tax Court keeps *legally binding* findings of fact completely secret, including from the Article III appellate courts required to review the Tax Court's judgments. At the same time, the majority below put itself into direct conflict with the D.C. Circuit on the legal relationship of the Tax Court to its special trial judges. There are no factual issues in dispute: the government defends, in principle, the position that the Tax Court may deny the courts of appeals and taxpayers ac-

cess to the findings and credibility judgments of special trial judges who preside over some of the Tax Court's lengthiest and most complex trials.

STATEMENT

1. Structure of the Tax Court. Congress established the United States Tax Court as an Article I "court of record." 26 U.S.C. § 7441. Congress has also given the Tax Court many of the same powers as the federal district courts. Just as the District Courts may appoint magistrates, the Chief Judge of the Tax Court "may, from time to time, appoint special trial judges * * *." 26 U.S.C. § 7443A(a). Special trial judges (STJs) are at-will employees appointed at the discretion of the Chief Judge. They have no statutory term of office and serve at the pleasure of the Tax Court. See 26 U.S.C. § 7443A.

Nonetheless, STJs wield considerable substantive powers and, unlike law clerks or secretaries, are far from mere employees. STJs exercise "significant governmental authority" and for that reason are "inferior officers" of the United States whose appointment must comply with the requirements of Article II of the Constitution. *Freytag v. Comm'r*, 501 U.S. 868, 880-882 (1991). Special trial judges exercise "judicial, rather than executive, legislative, or administrative, power," *Freytag*, 501 U.S. at 890-891, because the Tax Court "exercises judicial power to the exclusion of any other function." *Freytag*, 501 U.S. at 868. The Chief Judge of the Tax Court may assign any proceeding to a STJ for trial. 26 U.S.C. § 7443A(b). Currently, there are 19 Tax Court judges and 10 special trial judges.

In several classes of trials, Congress has authorized STJs to issue the final decision of the Tax Court. 26 U.S.C. § 7443A(c). But in financially significant cases, such as this one, where the claimed deficiency exceeds $50,000, trials before an STJ are governed by the special procedures set forth in Tax Court Rule 183. That Rule makes the STJ the

original finder of fact. After trial, the STJ is legally required to "submit a report, including findings of fact and opinion" to the Chief Judge of the Tax Court. Tax Ct. R. 183(b). As this Court has observed, the special trial judge "hear[s] the case and prepare[s] proposed findings and an opinion." *Freytag*, 501 U.S. at 873.

The Chief Judge then assigns a Tax Court Judge to review this Rule 183 report. *Id.* Critically, Rule 183 expressly requires that, in reaching its final decision, the Tax Court must give appropriate deference to the fact that the special trial judge has seen the witnesses, is in the best position to judge their credibility, and has presided over the entire trial. Rule 183(c) therefore mandates that "[d]ue regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Before this case, the lower courts and the Tax Court bar had understood this provision to mean that the special trial judge's findings of fact are to be overturned only if clearly erroneous. See, *e.g.*, *Landry v. FDIC*, 204 F.3d 1125 (D.C. Cir. 2000); *Stone v. Comm'r*, 865 F.2d 342 (D.C. Cir. 1989); 35 AM. JUR. 2d *Fed. Tax Enforcement* § 905 (2002) ("The Tax Court is required to review a special trial judge's factual findings according to the clearly erroneous standard."); 20A FEDERAL PROCEDURE, L. ED., INTERNAL REVENUE § 48:1274 (2000) (same).

A Tax Court judge reviews the trial judge's Rule 183 report. Rule 183(c) provides: "The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions." Tax Ct. R. 183(c). That power to modify, of course, is subject to the constraints of the Rule that require respect for the crediblity

judgments of the STJ and that the STJ's findings "shall be presumed to be correct."

2. The Tax Court's Secret Process of Decisionmaking. The Tax Court treats the STJ's legally required Rule 183 report as a secret document not to be disclosed under any circumstance, including to the courts of appeals. That is so even though the Tax Court itself is expressly bound to treat the factual findings of the trial judge, including credibility findings, as presumptively correct. In this tax fraud case, issues of intent, and hence trial-judge findings on credibility, were critical. Yet even though the actual (but secret) record of decisionmaking in the Tax Court legally depended upon the Rule 183 report, the record upon which the court of appeals was permitted to review the Tax Court decision did not include that report or the trial judge's original findings.

The Tax Court, in a reversal of earlier policy, now takes the position that, as a per se matter, it will refuse to make the trial judge's report part of the record. Even in a civil tax fraud case where credibility findings are critical, neither the taxpayer, nor the government, nor the courts of appeals — even *in camera* — are permitted to see the trial judge's Rule 183 report or to review the full record underlying the Tax Court's decision. As Judge Cudahy observed below, the Tax Court is "unique among all the institutions in the law" in claiming the power to refuse to disclose the "presumed correct" findings of fact of a trial judge or hearing officer. App. 71a.

But the Tax Court process is even more remarkable than the "mere" non-disclosure of the trial judge's original findings. For the Tax Court then may choose to alter the public record of decision. After the trial judge files the legally binding Rule 183 report, the Tax Court permits the reviewing judge and the trial judge to discuss the findings of fact and credibility judgments. If the reviewing judge disagrees with the trial judge's findings, the reviewing judge can privately

"persuade" the trial judge (employed at the will of the Tax Court) to sign a new opinion with completely modified findings. Only that new opinion is ever made part of the record.

Any reversal the Tax Court makes of the "presumed correct" and legally binding factual findings recorded in the Rule 183 report is therefore never reflected in the record. If any changes have been made, there is no way for the courts of appeals or the taxpayer to know. Whether the Tax Court has properly followed the requirements of Rule 183 is impossible to review. Whether the findings of fact in the newly minted Tax Court opinion are clearly erroneous is impossible properly to judge. Absent the Rule 183 report, it is impossible for the courts of appeals to evaluate the Tax Court's decision in the appellate manner prescribed by law.

In contrast to this current process, before 1983 the Tax Court's rules *required* the disclosure in every case of the STJ's report. See Tax Ct. R. 182(b), 60 T.C. 1149 (1973). But in that year, the Tax Court amended the rule to eliminate mandatory, routine disclosure of the trial judge's report. See 81 T.C. 1069 (1983) (amending the Rule and renumbering it as Rule 183). The Tax Court offered no explanation at the time for this change. The powers of the STJ and the reviewing judge remained exactly the same as before. But the Tax Court simply dropped, without explanation, the provision mandating public disclosure of the STJ report.

There is yet one further remarkable feature to this process: the entire process is itself shrouded in secrecy. Nowhere does the Tax Court make public or describe the fact that its judges claim the power to modify *outside the record* legally binding and "presumed correct" original findings of fact, including credibility judgments. Neither Rule 183 nor any document of the Tax Court indicates that the final decision of the Tax Court — the only document disclosed — might contain dramatically altered findings of fact.

To the contrary, the Tax Court gives the appearance in every case that no such modifications have been made. The final decision of the Tax Court always begins with a boilerplate statement that the Tax Court judge "agrees with and adopts the *opinion* of the Special Trial Judge." See App. 3a, 98a (emphasis added). Following that statement is an opinion issued in the name of the STJ. But as the government concedes, that "opinion" is not necessarily the Rule 183 report with its original findings of fact. See Gov't Brief in Opposition, *Ballard v. Comm'r* ("*Ballard* Opp."), No. 03-184, at 13 n.3 (filed Oct. 6, 2003) (acknowledging that the boilerplate language in Tax Court opinions might reflect the current "views" of the STJ, not the original findings, and that those original findings might have been "revised"). As Judge Cudahy concluded, "I do not believe that the concealment behind that [boilerplate] verbal formula allows this court to conduct meaningful appellate review." App. 96a-97a.

As became clear in the proceedings below, this boilerplate "adoption" of the STJ's "opinion" is language found in *every reported Tax Court opinion in a case tried by a Special Trial Judge* since repeal in 1983 of the Rule requiring publication of the trial judge's report. See App. 73a. "[T]here exists not a single Tax Court decision since the adoption of current Rule 183 where a Tax Court Judge has purported to modify or reverse a finding of a Special Trial Judge." *Id.* Before 1983, Tax Court decisions would expressly state that "we disagree with the Special Trial Judge,"[1] or that the Tax Court had made "some modifications" to the trial judge's report.[2] But once the Tax Court closed off access to the trial judge's report, the Tax Court never again manifested public disagreement with its STJs. As Judge Cuhady concluded, and the government does

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[1] See, *e.g.*, *Rosenbaum v. Comm'r*, 45 T.C.M. (CCH) 825 (1983), *rev'd sub nom. Stone v. Comm'r*, 865 F.2d 342 (D.C. Cir. 1989).

[2] See, *e.g.*, *Taylor v. Comm'r*, 41 T.C.M. (CCH) 539 (1980).

not dispute, that public show of unanimity on every factual finding in every case over two decades reflects either unique agreement among judges or, more realistically, that the Tax Court is modifying original findings of fact through an unreviewable process that leaves no trace in the public record. App. 74a. As commentators have learned of this practice, they have urged that it violates due process.[3]

3. Tax Court Proceedings in This Case. Burton W. Kanter was one of the leading estate-tax lawyers in the country, a prolific writer on tax planning, and an adjunct professor of law for nearly 15 years at the University of Chicago Law School. Kanter and others sought review in the Tax Court of notices of deficiency that, with interest and penalties, totalled more than $30 million. The notices did not determine fraud, but the Commissioner later amended his answer to allege fraud.

The Chief Judge of the Tax Court assigned the trial to Special Trial Judge Couvillion. That trial before Judge Couvillion consumed five weeks and "generated almost 5000 pages of transcript, more than 4600 pages of briefs and thousands of exhibits consuming hundreds of thousands of pages." App. 3a.

As required by law, Judge Couvillion prepared and filed a Rule 183 report. Filed more than four years after trial, that report, by law, included findings of fact, critical judgments of credibility, and legal conclusions on the issue of fraud. The Chief Judge then assigned the report for review to Tax Court Judge Dawson. App. 113a-114a. The report was under review by Judge Dawson for one year and three months. After

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[3] See, *e.g.*, Cornish F. Hitchcock, *Public Access to Special Trial Judge Reports*, 2001 Tax Notes Today 199-41 (Oct. 15, 2001); Gerald A. Kafka & Jonathan Z. Ackerman, *Fact-Finding in the Tax Court: Access to Special Trial Judge Reports*, 91 Tax Notes 639, 642 (April 23, 2001).

that lengthy period, Judge Dawson issued the Tax Court's decision, in which Kanter was found liable for tax fraud.

Two judges of the Tax Court later came forward to inform Tax Court counsel that Judge Dawson's decision had completely reversed the critical findings of credibility and the ultimate judgment of tax fraud of the trial judge in his Rule 183 report. These declarations are reflected in uncontradicted testimony in the record.[4] These two Tax Court judges (one a regular Tax Court judge, the other the Chief Special Trial judge) informed counsel:

> ¶4 * * * [I]n his original report submitted to the Chief Judge pursuant to Rule 183(b), Special Trial Judge Couvillion concluded that payments made by the [taxpayers] were not taxable to the individual Petitioners and that the fraud penalty was not applicable.
>
> ¶5 * * * That substantial sections of the opinion were not written by Judge Couvillion, and that those sections containing findings related to the credibility of witnesses and findings related to fraud were wholly contrary to the findings made by Judge Couvillion in his report. The changes to Judge Couvillion's findings relating to credibility and fraud were made by Judge Dawson.

A third judge of the Tax Court confirmed that Judge Dawson "had made an outright rejection of credibility findings made by a Special Trial Judge." *Id.* ¶7.

Thus, the trial judge had found Kanter credible and not guilty of tax fraud. The reviewing judge reversed those findings. But the record does not reflect that reversal, nor does it

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[4] See *Declaration of Attorney Randall G. Dick*, Seventh Cir. App. 250-252; see also App. 73a n.1 (*Declaration* cited in Judge Cudahy's dissent). Tax Court counsel did not raise these statements in the first two motions seeking the trial judge's report. Only after the Tax Court denied these motions did counsel, in a final motion, believe himself ethically required to file an affidavit testifying to these statements.

explain or justify (under any standard of review) the reversal of these critical findings. Instead, the final decision simply concludes: "Kanter's testimony at trial was implausible, unreliable, and sometimes contradictory. We did not find it credible." *Inv. Research Assocs., Ltd. v. Comm'r*, 78 T.C.M. (CCH) 951, 1085 (1999). But the court of appeals could not review this dispositive finding of Judge Dawson with the knowledge that he had *reversed* critical credibility judgments by the trial judge who had seen the witnesses. The court also could not evaluate and review any basis Judge Dawson might have had for reversing these findings.

Instead, Judge Dawson's opinion began with the standard boiler-plate statement that he "agrees with and adopts the *opinion* of the Special Trial Judge." App. 98a (emphasis added). But this misleading language does *not* mean that Judge Dawson adopted the original Rule 183 Report that STJ Couvillion submitted. The government, before this Court, concedes as much. See *Ballard* Opp. at 13 n.3. In the 15 months the Rule 183 Report was before Judge Dawson, he and the trial judge could have "agreed" to any number of changes in findings, none of which are reflected in the record. Judge Dawson's boiler-plate statement indicates no more than that he adopted the final views of the trial judge, as those views were modified from the original Rule 183 findings by whatever discussion Judge Dawson and the trial judge had subsequent to the filing of that report.

The Tax Court refused, in response to three separate motions, to have the special trial judge's report released or made part of the record, even for *in camera* appellate review. App. 99a, 104a, 107a. As Judge Cudahy put it dissenting below, "[t]he Tax Court has not denied that a document containing the original findings of the STJ exists, yet it refuses to include this document in the record on appeal." App. 71a.

4. The Seventh Circuit's decision. A divided panel of the court of appeals affirmed.[5] The majority upheld the Tax Court on two grounds. First, the court concluded that "the Tax Court's opinion is the STJ's report" and hence that petitioner's constitutional claims were "moot" and "immaterial." App. 7a. But this conclusion reflected understandable confusion, due to the Tax Court's opaque and hidden process, about the now acknowledged fact that the Tax Court's opinion is *not* necessarily the STJ's report. Even the Government no longer defends the Tax Court's actions on this basis, see *Ballard* Opp. at 13 n.3, and given this concession, this ground can no longer properly sustain the judgment below. The government acknowledges that the Tax Court's decision might have dramatically changed the findings and credibility judgments in the original trial judge report.[6]

Alternatively, the court of appeals held that "even if * * * the phrase 'agrees with and adopts' masks what is in fact a quasi-collaborative judicial deliberation in which an STJ's initial findings are malleable," App. 7a, neither due

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[5] Appeals from the Tax Court are taken to the Circuit in which the taxpayer legally resides. The parties before the Tax Court resided in three different Circuits. In *Estate of Lisle v. Comm'r*, 341 F.3d 364 (5th Cir. 2003), the Fifth Circuit reversed as clearly erroneous the finding of fraudulent intent with respect to one of the taxpayers. The Eleventh Circuit affirmed the judgment of the Tax Court in *Ballard v. Commissioner*, 321 F.3d 1037 (11th Cir. 2003). A petition for certiorari in that case is now pending. See 72 U.S.L.W. 3129 (U.S. Aug. 4, 2003) (No. 03-184).

[6] This was the only ground relied upon by the Eleventh Circuit for its judgment in the *Ballard* case in which certiorari is now pending. There the court said "Petitioners-Appellants' arguments are premised upon the assertion that the underlying report adopted by the Tax Court is not, in fact, Special Trial Judge Couvillion's report. Were that to be the case, we, too, would have significant concerns over the propriety of the process employed in this case." 321 F.3d at 1042. The candid refusal of the government now to claim that the Tax Court *has* adopted Judge Couvillion's report without modification leaves the *Ballard* decision without any support.

process nor applicable federal statutes are violated when the Tax Court changes "malleable" trial-judge findings without the record reflecting or justifying those changes.

The foundation of this conclusion was the court's view that Rule 183 imposes virtually no constraint on the reviewing powers of the Tax Court judge. In direct conflict with the D.C. Circuit's view that the Rule imposes a "clearly erroneous" internal standard of review, the court below concluded that the Tax Court Rules do not "prescribe any particular level of deference due the STJ's report." App. 8a. Moreover, the court noted that the final decision is signed by both the Tax Court judge and the STJ. Thus, both judges must have "agree[d]" on whatever secret revisions to findings were made. App. 7a. The court acknowledged that this Court's due process precedents would not permit a District Court to overturn a magistrate's original credibility findings in a suppression-hearing context through a similar, private, collaborative, non-record process. But the court concluded that the multi-million dollar property and liberty interests at stake in a tax fraud trial were not weighty enough to warrant constitutional concern about off the record modifications to critical credibility findings.

Judge Cudahy dissented at length. He concluded that any changes a reviewing judge makes to original findings of the trial judge must be reflected in the record to preserve the review function of the courts of appeals and the due process rights of taxpayers. By law, the courts of appeals are required to review Tax Court decisions, including findings of fact for clear error. The courts of appeals must therefore be able to evaluate the basis for the Tax Court's findings.

Judge Cudahy relied on this Court's analysis of the "clear error" standard of review in cases such as *Anderson v. City of Bessemer City*, 470 U.S. 564, 573-575 (1985) (clear error standard requires significant deference to factfinder's findings and "even greater deference" when credibility is in-

volved). App. 89a-90a. Without access to the original report, Judge Cudahy concluded, it is impossible for the reviewing court properly to assess critical elements of the Tax Court's decision. As Judge Cudahy summarized, "[i]f we are to give 'even greater deference' to the findings of a judge who has heard the witness whose credibility is at stake, we must inevitably give less deference to the judge who subsequently reverses those findings." App. 90a. Yet without the trial judge's original report, it is impossible to identify which findings he has made and which have been reversed by the Tax Court judge. The Tax Court's practice therefore destroys "meaningful" appellate review. App. 89 n.10. Judge Cudahy concluded that the Tax Court's reliance on secret STJ reports violated due process.

REASONS FOR GRANTING THE PETITION

This case involves a circuit split implicating recurring issues of immense practical and national importance. In cases from the Tax Court tried to a Special Trial Judge, the courts of appeals must review the Tax Court decision on a record that *omits* the single item of most significance. Over the last decade, Special Trial Judges have tried as many as 89 cases per year and, on average, at least 50 cases per year through the extraordinary, secretive process at issue here. These cases often involve enormous financial consequences. In *Freytag*, the amount at stake was $1.5 billion. 501 U.S. at 871 n.1. The present case involves a judgment in excess of $30 million in liabilities, penalties, and interest, as well as the additional consequences that attend a judgment of tax fraud.

The issues presented take on particular urgency following this Court's delineation of the powers of Tax Court special trial judges in *Freytag*. By holding that the Tax Court may assign any trial, "regardless of complexity and amount," to a STJ, *Freytag* spawned an expansion in the use of Special

Trial Judges in the Tax Court's largest cases.[7] The courts of appeals are now reviewing these judgments on the basis of incomplete records and secret trial judge reports, without being aware of that fact.

This Court should ensure that the regular practice of the Tax Court meets the minimal standards of due process, including proper appellate review, required of every other lower court. This Court's review is also justified to enforce Congress's mandate, expressed in the strongest terms in several statutes, that Tax Court proceedings must be fully transparent. At the same time, the decision below also creates a conflict among the circuits that warrants this Court's resolution.

I. SECRET TRIAL JUDGE FINDINGS OF FACT VIOLATE DUE PROCESS AND THE FEDERAL STATUTES THAT GOVERN THE TAX COURT.

The decision below holds it constitutional for a court to employ initial factfinders at trial, but then to keep secret the findings those judges officially make. That position conflicts with this Court's decisions on the minimal due process requirements of proper adjudicative process and on the deference owed to initial finders of fact on matters of credibility. In addition, the Tax Court practice contradicts the plain language of congressional statutes enacted to ensure full transparency of Tax Court decisionmaking.

A. Kanter's Due Process Rights Were Violated.

Secret trial judge reports violate this Court's central precedents on the constitutional role of credibility judgments, factfinding, and appellate review in judicial and administra-

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[7] In the 5 years before *Freytag*, the Tax Court used special trial judges an average of at least 41 times per year in cases of the type at issue here. In the 10 years after, this increased to at least 75 times per year. The cases involved are financially the largest the Tax Court decides through the use of STJs. See 26 U.S.C. § 7443A(b)(4); Tax Ct. R. 183.

tive processes. See *Anderson v. City of Bessemer City*, 470 U.S. 564 (1985); *United States v. Raddatz*, 447 U.S. 667, 677 (1980); *Universal Camera Corp. v. NLRB*, 340 U.S. 474 (1951). The final decision of the Tax Court depends by law on an undisclosed trial judge's report that has legally operative effect under the "due regard" standard of Rule 183. Failure to include that report in the record violates a taxpayer's due process rights to a fair initial trial and proper appellate review. See *Evitts v. Lucey*, 469 U.S. 387, 393 (1985) (applying due process to rights on appeal); *Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 429 n.5 (1982) (once access to courts is a legislative entitlement, government "may not deprive someone of that access unless the balance of state and private interests favors the government scheme"); *Concrete Pipe & Prods. of Cal., Inc. v. Constr. Laborers Pension Trust for S. Cal.*, 508 U.S. 602, 618 (1993) (due process requires "a[n] * * * adjudicat[ion]").

To prove fraud, the government was required to establish by clear and convincing evidence an intent of the taxpayer to defraud the government. App. 19a. Judgments of witness credibility are exceptionally important when fraudulent intent is at issue. Sixty witnesses testified at this lengthy trial; the trial judge directly questioned 40 of them. Particularly in such a context, as Judge Cudahy observed, "[t]he detailed interconnection of the credibility of different witnesses on different factual issues makes the accumulated impressions of the presiding officer irreplaceable." App. 93a. Indeed, Judge Cudahy concluded that the report the Tax Court keeps secret would be the single most important element in a proper review process by the appellate courts: "I can think of no single item of more significance in evaluating a Tax Court's decision on fraud than the unfiltered findings of the STJ who stood watch over the trial." *Id.*

The failure to include in the record these findings, the item of greatest significance to appellate review, constitutes an immediate and obvious violation of due process. A con-

stitutionally proper appeal must be based on a record that contains all the relevant information, including, in cases like this, the trial judge's findings of fact upon which the decision under review was required to be based and to which the reviewing court owes deference. Certain elements of a judicial process are so central to fair adjudication that their absence compromises fair process without the need for any further balancing of costs and benefits. A "neutral and detached judge in the first instance" is one. *Ward v. Village of Monroeville*, 409 U.S. 57, 62 (1972). The right to "some form of hearing" before the government infringes property rights is another. *Bd. of Regents v. Roth*, 408 U.S. 564, 570-571 n.8 (1972). The state's extinguishment of a cause of action without "the opportunity to present [the] case and have its merits fairly judged" is another. *Logan*, 455 U.S. at 433-434. When constitutionally protected property and liberty interests are at stake, as here, failure of the record on review to include those initial findings on which a lower court's final decision must, by law, depend is similarly a per se violation of due process. Otherwise, a reviewing court required to engage in "clearly erroneous" review cannot, as Judge Cudahy confessed, perform its adjudicative function. Taxpayers cannot be deprived of the right to adequate appellate review because, through no actions of their own, the Tax Court refuses to provide the full record of its decision to the appellate courts.

This common-sense conclusion is reinforced if one analyzes the question under the more formal due process framework of *Mathews v. Eldridge*, 424 U.S. 319 (1976), as Judge Cudahy did below. App. 83a-84a. *Mathews* requires the Court to weigh (1) the private interests at stake; (2) the effect on decisionmaking accuracy of the procedure at issue; and (3) the public interests implicated. *Mathews*, 424 U.S. at 335. Parts (1) and (3) are straightforward here. The private interests in a civil tax fraud trial for massive liability are substantial; only a criminal trial would involve weightier private interests. Conversely, the public costs of requiring the Tax

Court to disclose to the appellate courts the Rule 183 report are obviously minimal. This report must already be prepared and filed with the Tax Court; for years, the Tax Court routinely disclosed the report.

The effect of disclosure on enhancing decisionmaking accuracy is self-evident. Indeed, the importance of disclosure of the findings of the judge who held the trial, heard the witnesses, and was required by law to make findings of fact is emphasized repeatedly in this Court's decisions on the legal role of factfinding and credibility judgments, as well as by long-established judicial practice. See, *e.g.*, *Honda Motor Co. v. Oberg*, 512 U.S. 415, 430 (1994); cf. *Burnham v. Superior Court*, 495 U.S. 604, 609 (1990) (plurality opinion of Scalia, J., joined by Rehnquist, C.J., and Kennedy and White, JJ) ("due process 'mean[s] a course of legal proceedings according to those rules and principles which have been established in our system of jurisprudence for the protection and enforcement of private rights'") (quoting *Pennoyer v. Neff*, 95 U.S. 714, 733 (1878)).

Disclosure of the findings of a trial judge, hearing officer, or analogous initial factfinder is indeed such a fundamental premise of proper judicial (and even administrative) process that petitioner has been unable to find *any* area in modern federal law where such disclosure is not routine. Nor has the government identified any area where secrecy of this kind is accepted. Just as the Tax Court can assign special trial judges to try cases, the district courts can employ magistrates as adjunct factfinders. Congress has required that the report of a magistrate judge be served on the parties and be part of the record. 28 U.S.C. § 636(b)(1)(C). That is so even though the district court has greater authority on review than does the Tax Court. A district court can make de novo findings when objection is taken to magistrate findings. 28 U.S.C. § 636(b)(1). Similarly, a bankruptcy judge's initial findings of fact are part of the record and cannot be set aside in the district court unless clearly erroneous; the district

court, like the Tax Court, must also give "due regard" to the opportunity of the bankruptcy court to judge the credibility of the witnesses." Fed. R. Bankr. P. 8013. The reports of Special Masters must be filed with the clerk of the court and the parties notified of these reports. Fed. R. Civ. P. 53(e)(1).

Though administrative agencies are typically held to lesser standards of formal process than courts, such as the Tax Court, even federal agencies are required always to disclose original findings of fact. The Administrative Procedure Act (APA) requires that the record on review include any preliminary findings from a hearing officer or administrative law judge, regardless whether the agency has de novo power over facts. 5 U.S.C. §§ 557(b), 706. The framers of the APA considered this a critical requirement of properly structured decisionmaking, particularly "on matters which the hearing commissioner, having heard the evidence and seen the witnesses, is best qualified to decide * * *."[8] With respect to state administrative agencies, state courts have regularly held non-disclosure of a hearing officer's report to violate due process; as the leading case put it, without disclosure review "is like a performance of *Hamlet* without the Prince of Denmark." *Mazza v. Cavicchia*, 105 A.2d 545, 560 (N.J. 1954).[9] Judge Cudahy noted below that, "[w]hen a reviewing court reviews agency findings on credibility for substantial evidence, it is strongly influenced by the preliminary findings of

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[8] REPORT OF THE COMMITTEE ON ADMINISTRATIVE PROCEDURE, ADMINISTRATIVE PROCEDURE IN GOVERNMENT AGENCIES 51 (1941).

[9] *Mazza* was written by Arthur T. Vanderbilt, Chief Justice of the New Jersey Supreme Court. See BERNARD SCHWARTZ, ADMINISTRATIVE LAW 437 n.13 & n.14 (3d ed. 1991) (collecting cases following *Mazza* and state legislative provisions incorporating *Mazza*'s ruling). There a licensing board refused to disclose to the parties its hearing officer's report with proposed findings and conclusions. The court held due process violated, a holding endorsed by Professor Louis Jaffe. *See* Louis L. Jaffe, *Administrative Law Treatise*, 73 HARV. L. REV. 1638, 1640 n.4 (1960) (book review).

the ALJ who actually heard the witnesses — influence that becomes even more significant when an agency has reversed those preliminary credibility findings." App. 91a. Even for routine agency decisions, in which constitutionally-protected liberty and property interests are not at stake — and even when an agency has de novo factfinding power — Congress has concluded that accurate process requires the record to include initial findings of administrative officers and judges.

The facts in dispute here are not routine matters of historical or documentary record. They involve judgments of intent and credibility. This case highlights how essential the trial judge's original findings are to appellate review when credibility is at stake. The Fifth Circuit, in an opinion by Judge Higginbotham, has already held clearly erroneous the Tax Court's fraud judgment in this very case with respect to one of the purported "co-conspirators." *Estate of Lisle v. Comm'r*, 341 F.3d 364 (5th Cir. 2003). The Seventh Circuit likewise overturned as clearly erroneous one of the Tax Court's findings of fraud with respect to Kanter. App. 69a. In upholding the Tax Court's other findings, the Seventh Circuit *at least eight times* gave central importance to the Tax Court's purported judgments regarding Kanter's credibility or his "intent." Indeed, the divided panel held that "the lack of credibility of Kanter's testimony," which the Tax Court purportedly found, was a central justification for upholding the judgment of fraud. App. 18a. Yet the actual trial judge found that Kanter was in fact credible and had no intent to defraud.

Of all the findings that trial judges may make, this Court has recognized that special constitutional considerations apply when credibility judgments are at issue. *United States v. Raddatz*, 447 U.S. 667 (1980), involved suppression-hearings in which a magistrate had conducted the hearing and made credibility judgments. In that context, this Court suggested, and the lower courts consistently have concluded, that due process is violated if a district court overturns a magistrate's

findings on credibility without the district court itself hearing the witnesses. *Id.* at 681 n.7; see, *e.g.*, *Hill v. Beyer*, 62 F.3d 474, 482 (3d Cir. 1995); *In re Hipp, Inc.*, 895 F.2d 1503, 1519-1521 (5th Cir. 1990). Petitioner does not argue that the Tax Court should similarly be required to hear witnesses. But the constitutional interests at stake in a tax-fraud proceeding are sufficiently weighty that due process must, at a minimum, require that the record accurately reflect that the Tax Court has overturned findings of fact and credibility judgments of its trial judges.

In numerous other contexts, both judicial and administrative, this Court has also stressed the connection between accurate decisionmaking and deference to the credibility judgments of initial factfinders. See, *e.g.*, *Bessemer City*, 470 U.S. at 575 ("When findings are based on determinations regarding the credibility of witnesses, [the clearly erroneous standard] demands even greater deference to the trial court's findings * * *."); *Universal Camera Corp.*, 340 U.S. at 496 ("[E]vidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion. * * * The significance of [the presiding judge's or examiner's] report, of course, depends largely on the importance of credibility in the particular case."); *Concrete Pipe*, 508 U.S. at 623 ("the factfinder is in a better position to make judgments about the reliability of some forms of evidence than a reviewing body acting solely on the basis of a written record of that evidence. Evaluation of the credibility of a live witness is the most obvious example."). This Court's consistent emphasis on the special significance of credibility judgments highlights the constitutional infirmity in the Tax Court's practice of keeping the trial judge's report secret. Only with that report can the reviewing court assess any conflicts between the trial judge

and the reviewing Tax Court judge on credibility, where only the former has actually heard the witnesses.

In its related filing in the *Ballard* litigation, the government misconstrues the constitutional arguments in this case in three respects. First, citing *Morgan v. United States*, 298 U.S. 468 (1936), the government argues that the Tax Court need not personally observe the witnesses before making findings of fact contrary to those of the trial judge. But petitioner does not claim to the contrary. Petitioner's argument is that when, as here, the Tax Court's own rules *require* it to base its final decision, in part, on the trial judge's original findings, and to presume those findings correct, due process must then require that those findings *be part of the record* on review.

Second, the government argues that "there is nothing unusual about judges conferring with one another about cases assigned to them." Again, this is not what petitioners object to. But the Tax Court's own rules, like that of most judicial systems, differentiate between the role of initial factfinder and reviewing judge. Those rules require the trial judge to file a report of factual findings. The reviewing judge is to review that report. To be sure, the reviewing judge can modify those findings. If the reviewing judge is troubled about specific findings, he can direct the filing of additional briefs, receive further evidence, order oral argument, or recommit the report with instructions. Tax Ct. R. 183(c). But he is legally obligated to treat the trial judge findings as "presumed correct" and to give them "due regard," particularly on credibility. The record must therefore reflect any modification or rejection of these initial findings, if the appellate courts are to be able to determine whether the Tax Court has complied with its legal obligations. Discussion among Tax Court judges concerning pending cases is not the issue. The issue is the failure of the record to reflect whether the Tax Court has modified or reversed its trial judges' findings and, if so, on what basis.

Finally, the government notes that when a case has been tried by one judge of the Tax Court and is then reviewed by the full Tax Court, Congress has specified that the original decision shall not be part of the record. But in that context, the original decision has no legal effect at all on the final decision. By contrast, here the Tax Court's own rules accord the STJ report a specific legal role in the final decision. If the Tax Court must give that report deferential review when rendering a final decision, the court of appeals must have access to the report to properly perform its function and the parties must have access to protect their rights.

B. The Tax Court's Practice Violates Federal Statutes.

Section 7461(a) of the Revenue Code requires that "all reports of the Tax Court and all evidence received by the Tax Court * * * shall be public records." 26 U.S.C. § 7461(a). The STJ's Rule 183 report is such a report, as the plain language of Rule 183 itself recognizes. See Tax Ct. R. 183(b) (requiring filing of the "Special Trial Judge's Report"). Section 7461 permits the Tax Court to exempt from disclosure trade secrets or other confidential information. 26 U.S.C. § 7461(b). But the statute makes no similar exception for STJ reports. The Tax Court's regular practice of secret STJ reports thus violates the plain language of § 7461 and creates an additional exception where Congress chose to provide none. Similarly, § 7459(b) requires that "[t]he Tax Court shall report in writing *all* its findings of fact, opinions, and memorandum opinions." 26 U.S.C. § 7459(b) (emphasis added). Non-disclosure of the trial judge's original report violates this statute as well.

The history of § 7461 makes clear that Congress' strong textual insistence on full disclosure was no casual commitment. The entire motivation for this provision was to eliminate precisely the type of secrecy at issue here. Similar secrecy had been the hallmark of the Treasury Department's

adminstration of the tax law before prior versions of § 7461 were enacted. Congress acted specifically to transform the adjudication of tax disputes so that the government's decisionmaking would be transparent and accountable.

The publicity requirement in current § 7461 originated in the Revenue Act of 1924, which established the Board of Tax Appeals (the "Board"), predecessor to the Tax Court. Since then, the statute's requirement that all hearings and reports by the Board are public records has been largely unchanged. The original bill reported by the Senate Committee on Finance did not contain any publicity requirement. That absence provoked the dissenting minority on the committee, through Senator Jones, to demand an amendment:

> Controversies between the Government and the taxpayers extending into many thousands and involving revenue of many hundreds of million of dollars are required to be annually adjudicated. * * * Under the present practice all of these adjudications are made in secret. An opportunity is afforded for favoritism, arbitrary action, fraud, and collusion. * * * The majority proposes that all records and proceedings of the Internal Revenue Bureau shall remain secret as in the past. To the minority it seems inconceivable that any controversy existing between the Government and a taxpayer should be adjudicated and finally determined in a star chamber proceeding. The minority will, therefore, propose an amendment to the bill which will provide that *all such proceedings, records, and evidence in connection therewith shall be public.*

S. REP. NO. 68-398, pt. 2, at 12 (1924) (emphasis added). The amendment adopted contained the publicity requirement in essentially the same terms as in § 7461. The single purpose behind that amendment, as stated by Senator Jones, was to ensure that adjudication of tax disputes, in all phases, be made fully open to public and taxpayer scrutiny. This history

makes no distinctions among the kinds of hearings, proceedings, or records required to be open. Recognizing the special sensitivity of tax proceedings, Congress expressly required transparency for "*all* such proceedings, records, and evidence." *Id.* (emphasis added). The publicity requirement was designed to include not just the final determinations of the Board, but also all "records * * * in connection therewith." *Id.*

The congressional debates reiterated the aim of wholly eliminating secrecy in tax proceedings. "[T]he publicity placed upon [the Board's] activities are the result of the vicious secrecy system which has grown up in the Treasury Department under the present law." 65 CONG. REC. 9549 (1924) (statement of Rep. LaGuardia). The statute was designed to enhance the judicial character of tax proceedings, precisely to avoid the problems associated with secret executive decisionmaking in revenue disputes. See, *e.g.*, 65 CONG. REC. 7690 (1924) (statement of Sen. Reed). This was the congressional view long before Congress transformed the Tax Court into a formal Article I court in 1969.

There is no doubt that, were the Tax Court today an administrative agency, the report of the STJ would be both required to part of the record under the APA and to be disclosed under FOIA.[10] It would be perverse to conclude that, by creating the Tax Court as an Article I court, Congress permitted the Tax Court to refuse to disclose trial judge findings of fact that any agency would routinely be required to disclose — especially when Congress has long legislated to require more transparency of tax proceedings than other administrative proceedings. That national policy was further enhanced by the enactment in 1988 of the Taxpayer Bill of Rights. See Omnibus Taxpayer Bill of Rights, Pub. L. No.

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[10] See *Dep't of Justice v. Tax Analysts*, 492 U.S. 136, 147 (1989); see also *Kissinger v. Reporters Comm. for Freedom of the Press*, 445 U.S. 136, 157 (1980).

100-647, §§ 6226-35, 102 Stat. 3342, 3731 (1988). The purpose of this Act was to "ensure that we maintain basic due process rights [in tax disputes], which have eroded slowly but surely over these past two and one-half-decades." 134 CONG. REC. S4134-07 (April 15, 1988) (statement of Sen. Pryor).

That the Tax Court *is* an Article I court, not an administrative agency, is further reason for this Court to make clear that the Tax Court's regular practice of secret findings flaunts traditional, deeply established legal principle. American law has long recognized a common-law right of access to judicial records and documents. See, *e.g.*, *Nixon v. Warner Communications, Inc.*, 435 U.S. 589, 597 (1978). This right creates a strong presumption in favor of disclosure of all such records, a principle justified in light of "the citizen's desire to keep a watchful eye on the workings of public agencies." *Id.* at 598. Lower-courts also emphasize the common-law right of access to judicial documents that shed light on the bases for judicial decisions. See, *e.g.*, *Brown & Williamson v. FTC*, 710 F.2d 1165, 1181 (6th Cir. 1983) (noting public interest "in ascertaining what evidence and records the District Court and this Court have relied upon in reaching our decisions"); *Joy v. North*, 692 F.2d 880, 894 (2d Cir. 1982) (requiring that "a report" used in rendering judgment be revealed: "[s]ince it is the basis for the adjudication, only the most compelling reasons can justify the total foreclosure of public and professional scrutiny."). The STJ's report is more significant than documents that "might" merely have affected a judicial decision. That report contains findings required by law to be "presumed correct." If the press has a common-law right to judicial documents in general, the litigants most directly affected by the fairness of the Tax Court's adjudicative process must have a common-law right to the legally binding STJ report.

Given the number and significance of cases affected, this Court should clarify that the congressional statutes that gov-

ern the Tax Court must be construed against this longstanding historical "presumption" in favor of public access to judicial records. See *Nixon*, 435 U.S. at 602. The scope of the authority Congress delegated to the Tax Court to adopt rules of procedure, 26 U.S.C. §§ 7443A(a), 7453, must be interpreted against Congress's foundational rule that "all reports" of the Tax Court are "public records."

In addition, Congress has assigned the courts of appeals the duty to review "decisions" of the Tax Court "in the same manner and to the same extent" as decisions of the district courts in non-jury civil actions. See 26 U.S.C. § 7482. That appellate function must entail review of the record as a whole. The government notes that only "decisions" of the Tax Court are reviewed and the STJ's report is not itself such a "decision." *Ballard* Op. at 12-13. But this misunderstands the appellate review statute. To fulfill its statutory obligation to review the "decision" of the Tax Court, the court of appeals must be able to evaluate the complete record, including the STJ report, which provides the basis for that decision.

As the dissent below concluded, the Tax Court is regularly violating due process. This is another compelling reason for this Court to clarify that the governing statutes must be construed to mandate disclosure of the trial judge's report. See *Edward J. DeBartolo Corp. v. Fla. Gulf Coast Bldg. & Constr. Trades Council*, 485 U.S. 568, 575 (1988).

II. THIS CASE CREATES A CONFLICT AMONG THE COURTS OF APPEALS CONCERNING TAX COURT RULE 183(C).

The decision below rests squarely on a determination that Rule 183(c) does not require "any particular level of deference" on the part of the Tax Court to the findings and credibility judgments of the trial judge who presided over this five-week trial. App. 8a. That holding directly conflicts with the holding of the D.C. Circuit in *Stone v. Commissioner*, 865 F.2d 342 (D.C. Cir. 1989).

Stone decided the exact legal issue presented here: "the critical legal issue is the deference that the Tax Court owed the Special Trial Judge, to whom the matter was referred for fact-finding [on a certain date]." *Id.* at 344. *Stone* also addressed the exact same language at issue here, which at the relevant time was contained in Rule 182(d): "'Due regard shall be given to the circumstance that the commissioner [since re-named the special trial judge] had the opportunity to evaluate the credibility of witnesses; and the findings of fact recommended by the commissioner *shall be presumed to be correct.*'" *Id.* at 345 (quoting Tax Ct. R. 182(d), 60 T.C. 1150 (1973)) (emphasis in *Stone*).

Writing for the Court, Judge Williams relied on "the natural reading" of the Rule's text, the legislative history of the Rule, and the use of similar language in other areas of federal law. *Id.* at 347. *Stone* concluded that "the language of the Tax Court Rule applicable to this case (and still applicable under a different number) sought to establish the relatively high level of deference that the phrase 'clearly erroneous' entails." *Id.* at 344. Moreover, the D.C. Circuit expressly rejected the very argument put forward here, namely that the Rule requires no deference at all to the trial judge's findings or only a "mild presumption in favor." *Id.* *Stone* instead concluded that the terms "due regard" and "presumed correct" invoke "language with a reasonably well-established meaning." *Id.* at 347. The "natural reading" of the Rule imposes "[a] clearly erroneous standard" for Tax Court review of special trial judge findings of fact. *Id.*

Stone also involved precisely the same factual context as this case. In both cases, the Tax Court judges called no witnesses but nonetheless reversed its special trial judges, after lengthy and complex trials, on critical factual and credibility findings. *Stone* held the Tax Court decision to be clearly erroneous "in light of the deference that the Tax Court owed the Trial Judge." *Id.* at 344. Here the court of appeals *could not reach any conclusion about whether the Tax Court has*

been clearly erroneous in reversing its trial judge because the trial judge's findings are not part of the record.

The Seventh Circuit explicitly rejected the holding of *Stone*. The court below concluded that "to impose the * * * requirement that the Tax Court review an STJ's findings for clear error * * * would all but abdicate the Tax Court's original decisionmaking authority." App 8a. Thus, the Seventh Circuit held that the Rule (now renumbered as Rule 183) does not "prescribe any particular level of deference due the [Special Trial Judge's] report." *Id.* Yet in word-for-word identical terms, the plain language of current Rule 183 is exactly the same as that of its predecessor: "Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Tax Ct. R. 183(c).

In *Freytag*, this Court deferred consideration of the meaning of Rule 183 while noting the significance of this Rule for the entire structure of Tax Court adjudication. 501 U.S. at 874 n.3. That uncertainty should now be resolved, given the conflict among the circuits. As noted commentators have observed, lower-court conflicts concerning administration of the tax laws warrant this Court's resolution even more than most conflicts, see, *e.g.*, HENRY J. FRIENDLY, FEDERAL JURISDICTION: A GENERAL VIEW 161-163 (1973), due to the unique "'spillover effects' [of such conflicts] that encourage costly strategic behavior by both the government and taxpayers." REPORT OF THE FEDERAL COURTS STUDY COMMITTEE 264-265 (July 1, 1990) (Judge Richard A. Posner, Chairman).

The D.C. Circuit's interpretation, not that of the court below, is also correct. Unlike *Stone*, the court below made no reference to the history of the Rule's development, to the "well-established meaning" the legal terms "due regard" and "presumed correct" have in other contexts, or to the practices

of other courts which employ similar rules. Indeed, the court below did not even refer to the "natural reading" of the plain language of the Rule. The court below instead simply asserted that "we believe" Rule 183 does not adopt a "clearly erroneous" standard of review. App. 8a.

The government has acknowledged the direct conflict with *Stone*. In its filing in *Ballard*, the government takes direct issue with *Stone*, arguing that, "[c]ontrary to petitioner's contention, a regular judge of the Tax Court is not to limit his review of recommended findings of a special trial judge through application of a 'clearly erroneous' or other deferential standard of review." *Ballard* Opp. at 10-11. But the government seeks to avoid the claim of a circuit split by asserting that the 1983 procedural changes and renumbering of the Tax Court Rule — which did not change a single operative word in the substantive standard of review — nonetheless somehow dramatically changed that substantive standard. *Id.* at 11 n.2. But the 1983 rule change only addressed one issue of procedure: it eliminated (without explanation) the portion of the rule requiring publication of the STJ's Report. The plain language of the Rule *continues* to impose the exact same "due regard" and "presumed correct" constraints on Tax Court review.

The D.C. Circuit, accordingly, has rejected the argument the government makes here. *Stone* concluded that "[t]he Tax Court has since made minor changes in the rule and renumbered it as Rule 183(c), but the last sentence is unaltered." 865 F.2d at 345. Thus, the D.C. Circuit noted the 1983 procedural change regarding disclosure, but expressly concluded that such a change had no bearing on whether the Rule imposes a "clearly erroneous" standard of review. The D.C. Circuit has also continued to rely on *Stone* in recent cases long after the 1983 changes. See *Landry v. FDIC*, 204 F.3d 1125, 1133 (D.C. Cir. 2000).

Just as significantly, the tax bar for over a generation has, as a result of *Stone*, continued to understand Rule 183 to impose a "clearly erroneous" standard. "[T]here certainly appears to be some consensus in the literature that the Rule still embodies a clear error standard." App. 79a (citing sources). Thus, from the vantage point of the tax bar as well as the D.C. Circuit, there is a clear conflict between the "clearly erroneous" standard of *Stone* and the "no deference at all" standard of the court below. That conflict requires this Court's review.

III. THIS COURT'S SUPERVISORY POWERS SHOULD BE EXERCISED TO MAKE CLEAR THAT SECRET TRIAL JUDGE REPORTS VIOLATE ACCEPTED PROCESSES OF JUDICIAL DECISIONMAKING.

This case also urgently calls for an exercise of this Court's supervisory powers over the federal courts. That exercise is appropriate when the lower courts have "so far departed from the accepted and usual course of judicial proceedings, or sanctioned such a departure by a lower court * * *." Sup. Ct. R. 10(a). "The authority which Congress has granted this Court to review judgments of the courts of appeals undoubtedly vests us not only with the authority to correct errors of substantive law, but to prescribe the method by which those courts go about deciding the cases before them." *Lehman Brothers v. Schein*, 416 U.S. 386, 393 (1974) (Rehnquist, J., concurring); see also 28 U.S.C. § 2106. These supervisory powers focus on "the need to protect the integrity of the federal courts," see, *e.g.*, *United States v. Payner*, 447 U.S. 727, 736 n.8 (1980), and to secure "the public reputation of judicial proceedings." *Nguyen v. United States*, 123 S. Ct. 2130, 2139 n.17 (2003).

Nguyen addressed congressional statutes embodying a "weighty congressional policy" concerning "the proper administration of judicial business." The Court employed its

supervisory powers to invalidate the judicial practice at issue even without a showing of individual prejudice to the specific defendant. That approach should apply a fortiori to judicial proceedings in which the trial judge's findings of fact are kept secret to the actual prejudice of the ability of the courts of appeals to render a proper judicial decision.

The lower court's endorsement of secret Tax Court trial judge reports so far departs from the "accepted and usual" course of judicial proceedings — indeed, from the proceedings of every other court — as to warrant exercise of this Court's supervisory power. It works a violation of both due process and congressional statutes requiring publicity of all Tax Court proceedings and reports. Those statutes reflect a "weighty policy" concerning the "proper administration of judicial business" that should be enforced, if necessary, through this Court's supervisory powers.

Reversal of the decision below would promote the development of the law in a large category of cases involving some of the Tax Court's most significant proceedings. This Court should make clear that appellate review that lacks access to the findings of fact "presumed to be correct" of the trial judge unacceptably "departs from the accepted and usual course of judicial proceedings" and cannot be permitted.

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted.

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APPENDIX

United States Court of Appeals,
Seventh Circuit.

ESTATE OF BURTON W. KANTER, DECEASED,
JOSHUA S. KANTER, EXECUTOR, AND NAOMI KANTER,
Petitioners-Appellants,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee.

Nos. 01-4316, 01-4317, 01-4318, 01-4319,
01-4320, 01-4321, 01-4322, 02-1220.

Argued Sept. 4, 2002.
Decided July 24, 2003.

Rehearing and Rehearing En Banc
Denied Oct. 21, 2003.

Before FLAUM, Chief Judge, CUDAHY and KANNE, Circuit Judges.

PER CURIAM.

The Estate of Burton Kanter and Naomi Kanter appeal a decision of the Tax Court. This consolidated appeal deals with six out of forty-one separate issues decided by the Tax Court with respect to alleged deficiencies of the late Burton W. Kanter, his wife, Naomi Kanter, and related entities, as well as two additional post-trial issues. We affirm in part and reverse in part.

INTRODUCTION

The late Burton W. Kanter,[1] and various family entities associated with him, have been audited by the Internal Reve-

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[1] Burton W. Kanter died on October 31, 2001. His estate was subsequently substituted as the principal party to this litigation. In order to avoid semantic contortions, this opinion refers inter-

nue Service virtually, if not literally, every year since Richard Nixon was President. Kanter was a well-known and accomplished tax and estate lawyer. He graduated from the University of Chicago Law School. He had a very successful law practice beginning in 1956, founding what would eventually become the law firm of Neal, Gerber & Eisenberg. Among Kanter's clients was the Pritzker family of Hyatt Corporation fame. Kanter was also an accomplished businessman, with "extensive exposure" to a "good many public * * * [and] private companies." (Tr. at 5278.)[2] Kanter wrote extensively on tax-related subjects (originating a "Shop Talk" column in the Journal of Taxation), and was an expert on the subject of trusts and estate planning. *See, e.g.*, Burton W. Kanter & Michael J. Legamaro, *The Grantor Trust: Handmaiden to the IRS and Servant to the Taxpayer*, 75 TAXES 706 (1997); Sheldon I. Banoff & Burton W. Kanter, *LLC Announcements: Damage Control*, 80 J. TAX'N 255 (1994); Burton W. Kanter & Sheldon I. Banoff, *Tax Planning for the Elderly*, 70 J. TAX'N 191 (1989); Burton W. Kanter, *AARP – Asset Accumulation, Retention and Protection: Prelude to Transmission*, 69 TAXES 717 (1991); Burton W. Kanter, *Cash in a "B" Reorganization: Effect of Cash Purchases on "Creeping" Reorganization*, 19 TAX L. REV. 441 (1964). In the 1960s and 1970s, Kanter helped Hollywood finance movies through tax shelter arrangements, and was involved in the production of many major Hollywood films, including "One Flew Over the Cuckoo's Nest." The IRS's extraordinary attention to Kanter is understandable given that from 1979 to 1989 Kanter, the highly successful

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changeably to the current Petitioners collectively, the Estate of Burton W. Kanter individually and to the late Burton Kanter, as "Kanter."

[2] "Tr." refers to the transcript for the Tax Court trial. "App." will refer to the appendix to Petitioners' brief.

tax attorney, who hobnobbed with Pritzkers and Hollywood producers and who participated in countless extremely large and lucrative business ventures, reported a negative adjusted gross income each year on his federal tax return and paid no federal income taxes. (Tr. at 5290-91.)

This consolidated appeal involves Kanter's petitions for review of deficiencies assessed during the years from 1978 to 1986, which is itself only a portion of the original consolidated case tried by the Tax Court in 1994 – a trial that generated almost 5500 pages of transcript, more than 4600 pages of briefs and thousands of exhibits consuming hundreds of thousands of pages, and was eventually, five years later, distilled into a 606 page opinion covering forty-one separate issues. A thorough description of the entire factual background to this case can be found in the Tax Court's opinion. *Investment Research Associates, Ltd. v. Comm'r*, 78 T.C.M. (CCH) 951 (1999) [hereinafter *IRA*]. The trial was conducted by Special Trial Judge Couvillion, to whom the Tax Court had assigned the case under 26 U.S.C. § 7443A(b)(4). *See also* Tax Court Rule 180.[3] Under the Tax Court's rules, the Special Trial Judge (STJ) then submitted a report containing findings of fact and opinion to the Tax Court's Chief Judge, who then assigned the case to Tax Court Judge Dawson. *See* Tax Court Rule 183(b). Judge Dawson subsequently issued his opinion, which stated that the Tax Court "agrees with and adopts the opinion of the Special Trial Judge, which is set forth below." *IRA*, 78 T.C.M. (CCH) at 963. Of the forty-one issues decided by the Tax Court, six were appealed to this court:[4]

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[3] All Rule references are to the Rules of the United States Tax Court (Tax Court Rules) unless otherwise indicated.

[4] The Tax Court trial consolidated the petitions of Kanter and two other individuals (Lisle and Ballard) against whom the Commis-

1. **Fraud**: The Tax Court determined that Kanter (and two colleagues) helped individuals obtain business opportunities in exchange for payments that later were fraudulently diverted through a series of Kanter-controlled entities in order to disguise the payments' origins and lower the tax assessed on the income (by dividing it up and assigning parts of it to various entities claiming losses). Kanter concedes that there was an underpayment of taxes but disputes that the Commissioner was able to prove by clear and convincing evidence that the underpayment was due to fraud.

2. **Bea Ritch Trusts**: Kanter challenges the Tax Court's determination that capital gains reported in 1986 by the Bea Ritch Trusts (BRT) were properly taxable to Kanter under the grantor trust provisions of the Internal Revenue Code (IRC).

3. **Washington Painting**: Kanter challenges the Tax Court's refusal to allow him to deduct expenses he incurred during an aborted sale of a painting.

4. **1982 Bank Deposits**: Kanter challenges the Tax Court's determination of a deficiency for the year 1982 based upon an analysis of his bank deposits. He argues that the Commissioner failed to meet his burden to prove a deficiency, that the Tax Court erred in presuming the Commissioner's deficiency determination to be correct, and that in

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sioner assessed deficiencies. Under 26 U.S.C. § 7482(b)(1)(A), appeals from Tax Court decisions are reviewed by the U.S. Court of Appeals for the circuit in which the legal residence of the petitioner lies. Of the three petitioners, only Kanter's legal residence lies within the Seventh Circuit. Parallel appeals for the other petitioners are ongoing in the Fifth and Eleventh Circuits. During the pendency of this appeal the Eleventh Circuit issued its opinion. *Ballard v. Comm'r*, 321 F.3d 1037 (11th Cir. 2003).

any event the evidence Kanter presented at trial was sufficient to overcome any presumption of correctness.

5. **Equitable Leasing**: Kanter challenges the Tax Court's determination that payments from Equitable Leasing Company to Kanter entities were taxable commissions and not loans.

6. **Cashmere**: The Tax Court disregarded a series of transactions involving (a) the contribution of certain partnership interests to a shelf corporation (Cashmere) and (b) the subsequent installment sale of Cashmere's stock, the result of which was an immediate recognition of capital gain to Kanter on the partnership interests. Kanter argues that the transactions had economic substance and should not have been disregarded as an attempt to avoid the payment of federal income tax.

The remaining two issues in this appeal concern events after the conclusion of the Tax Court's trial. Beginning in April 2000, Kanter sought repeatedly to have the original report filed by the STJ placed in the record, or in the alternative made available for this Court's review *in camera*. Kanter alleged that informal conversations with two Tax Court judges had revealed that the issued opinion had undergone significant alterations from the original report filed by STJ Couvillion. The Tax Court denied all of Kanter's motions. Kanter appeals the Tax Court's refusal to produce the STJ's original report. The final issue concerns Kanter's wife's (Naomi's) efforts to seek innocent-spouse relief from the deficiencies levied against her husband's estate.

To make this very complex case easier to understand we have placed a brief statement of facts relevant to each issue immediately preceding that issue's analysis. We begin with the broadest (and least fact dependent) issue: whether the STJ's original report should have been made part of the record on appeal. Then we address the six transactional issues

from the Tax Court's decision. Finally, we address Naomi Kanter's post-trial motions.

The United States Courts of Appeals have exclusive jurisdiction to review decisions of the United States Tax Court. 26 U.S.C. § 7482(a)(1); *Seggerman Farms, Inc. v. Comm'r*, 308 F.3d 803, 805 (7th Cir. 2002).

I. The STJ's Report

Kanter's first argument is that the STJ's original report must be made a part of the record on appeal so that this court can determine whether the appropriate degree of deference had been paid to it by the Tax Court judge, whose opinion is before us. Kanter claims that informal conversations between his attorney and other Tax Court judges revealed that the STJ who presided over the trial of this case submitted a report that found Kanter credible and recommended rejection of much of the Commissioner's assessed deficiencies, specifically the fraud deficiency. Kanter argues that the STJ's report cannot be rejected by the Tax Court unless clearly erroneous, and that, without the STJ's report in the record, there is no way for this court to determine if proper deference was accorded it. Moreover, this secret and unaccountable process of review allegedly violates Kanter's due process rights. Kanter, relying on a Supreme Court case examining the relationship between U.S. district court judges and magistrate judges, argues that this quasi-collaborative process affords a Tax Court the opportunity to reverse an STJ's credibility findings without first hearing or seeing the witnesses itself – thus offending due process. *See United States v. Raddatz*, 447 U.S. 667, 681 n.7 (1980) (observing in *dicta* that in the criminal context a district court judge's reversal of a magistrate judge's credibility findings without the district judge hearing or seeing the witnesses would raise "serious questions"). Kanter argues that in addition, our review of the Tax Court's decision is unconstitutionally impaired by the omission of the STJ's report from the record. Kanter's chal-

lenge of the Tax Court's refusal to include the "original" STJ report presents questions of law that we review *de novo*. *Pittman v. Comm'r*, 100 F.3d 1308, 1312 (7th Cir. 1996).

Of course, Kanter's arguments are immaterial if the Tax Court's final opinion is the STJ's report. *See Ballard*, 321 F.3d at 1042-43. The Tax Court's final opinion clearly states that it "agrees with and adopts the opinion of the Special Trial Judge." *IRA*, 78 T.C.M. (CCH) at 963. The Chief Judge of the Tax Court, Judge Dawson, and Special Trial Judge Couvillion himself all signed that final opinion, and we take their statement at face value. Therefore, notwithstanding Kanter's attorney's declaration, we accept as true the Tax Court's statement that the underlying report adopted by the Tax Court was in fact Special Trial Judge Couvillion's. *See Ballard*, 321 F.3d at 1042-43. This renders moot all of Kanter's arguments.

But even if, as the dissent suggests, the phrase "agrees with and adopts" masks what is in fact a quasi-collaborative judicial deliberation in which an STJ's initial findings are malleable, neither the Tax Court's own rules of procedure, the Federal Rules of Appellate Procedure, nor Congress' scheme for appeals from Tax Court decisions would require the Commissioner to include the STJ's preliminary report as part of the appellate record. Furthermore, this purportedly quasi-collaborative process would not offend our notions of fundamental fairness, nor would due process require the inclusion of the report in the appellate record to preserve the fairness of our review.

First, it is clear that the Tax Court's own rules do not require the report to be disclosed to the parties or made part of the appellate record. To the contrary, its rules specifically preclude the report's disclosure. That the Tax Court has the power to prescribe its own rules of procedure is undisputed. *See* 26 U.S.C. § 7453; *Stone v. Comm'r*, 865 F.2d 342, 347 (D.C. Cir. 1989) ("The Tax Court is of course free to make

its own rules determining the relation between it and its Special Trial Judges."). Having exercised that rulemaking authority, the Tax Court no longer requires an STJ's report to be made available to the parties and, by extension, no longer allows those parties to file objections to it. *Compare* Tax Court Rule 182(b), (c), 60 T.C. 1149, (1973) (providing for service of the STJ's report on each party and allowing each party to file objections to the report's findings), *with* Tax Court Rule 183, 81 T.C. 1070, (adopted 1983) (noting that "[t]he prior provisions for service of the [STJ's] report on each party and for the filing of exceptions to that report have been deleted").

Neither do the Tax Court procedures prescribe any particular level of deference due the STJ's report. Under the current rule, the Tax Court maintains sole authority to decide cases assigned to an STJ. Tax Court Rule 183(c) ("The Judge to whom or the Division to which the case is assigned may adopt the [STJ's report] or may modify it or may reject it in whole or in part * * *."); *see also Freytag v. Comm'r*, 501 U.S. 868, 875 n.3 (1991) ("[A] special trial judge has no authority to decide a case assigned under [§ 7443(b)(4)]."). The Tax Court thus acts as the original finder of fact. Conversely, the STJ's inability to decide cases limits the amount of deference that the Tax Court, as the original factfinder, must pay to those preliminary findings. Although the Rule requires that "due regard" be given to the STJ's opportunity to evaluate the credibility of witnesses and that those findings be presumed correct, *see* Tax Court Rule 183(c), to impose the further requirement that the Tax Court review an STJ's findings for clear error, as Kanter urges, would all but abdicate the Tax Court's original decisionmaking authority. Instead, we believe Rule 183's due-regard language merely instructs the Tax Court to be cognizant that the STJ had the opportunity to evaluate the credibility of witnesses, and allows the Tax Court to overcome the presumption of correct-

ness it prescribes should it find that the evidence suggests those findings were incorrect. Consequently, secreting the report does not offend any rule-mandated check on the Tax Court's power to decide cases assigned to an STJ.

Second, Congress has by statute precluded direct appellate review of STJ reports. We lack jurisdiction to review anything but "decisions of the Tax Court." 26 U.S.C. § 7482(a)(1). We have repeatedly held that the use of the term "decisions" in § 7482 means that the appellate courts can review only (i) dismissals (e.g., for lack of jurisdiction) or (ii) formal determinations of deficiency (or lack thereof). *See, e.g., Kreider v. Comm'r*, 762 F.2d 580, 584 (7th Cir. 1985). In other words, a "decision" of the Tax Court is the final formal ruling of the Tax Court; a preliminary "report" is not a decision. *See* 26 U.S.C. § 7459(a) ("A *report* upon any proceeding instituted before the Tax Court and a *decision* thereon shall be made as quickly as practicable. The *decision* shall be made by a judge in accordance with the *report* of the Tax Court, and such *decision* so made shall, when entered, be the *decision* of the Tax Court." (emphasis added)). An STJ report, therefore, is not reviewable, *see Estate of Smith v. Comm'r*, 638 F.2d 665, 670 (3d Cir. 1981), which lends credence to the Commissioner's argument that Congress intended STJ reports to be treated as preliminary findings comprising part of the Tax Court's internal deliberative process.

Third, the Federal Rules of Appellate Procedure do not require that STJ reports be made part of the statutorily required record on appeal of a "decision" of the Tax Court. Federal Rule of Appellate Procedure 14 excepts appeals of Tax Court decisions from certain rules of appellate proce-

dure.[5] Among those rules not applicable to Tax Court review is Rule 16, which provides that the record on review of an administrative order shall include "any findings or report on which [the order] is based." Fed. R. App. P. 16(a)(2). Unlike other administrative actions, the Federal Rules of Appellate Procedure thus do not require that Tax Court decisions be reviewed in light of the preliminary findings upon which the decision was based. Instead, Rule 13 notes that Rule 10 governs the contents of a Tax Court appellate record, and that rule does not require the record to include any preliminary findings or reports. Fed. R. App. P. 13 & 10(a).[6]

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[5] Federal Rule of Appellate Procedure 14 states that "[a]ll provisions of these rules, except Rule 4-9, 15-20, and 22-23, apply to review of a Tax Court decision." Fed. R. App. P. 14.

[6] Federal Rule of Appellate Procedure 13 provides in relevant part:

> (d) *The Record on Appeal; Forwarding; Filing.*
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> (1) An appeal from the Tax Court is governed by the parts of Rules 10, 11, and 12 regarding the record on appeal from a district court, the time and manner of forwarding and filing, and the docketing in the court of appeals. References in those rules and in Rule 3 to the district court and district clerk are to be read as referring to the Tax Court and its clerk.

Fed. R. App. P. 13(d)(1). And Federal Rule of Appellate Procedure 10 provides in relevant part:

> (a) *Composition of the Record on Appeal.* The following items constitute the record on appeal:
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> (1) the original papers and exhibits filed in the district court;
>
> (2) the transcript of proceedings, if any; and
>
> (3) a certified copy of the docket entries prepared by the district clerk.

Fed. R. App. P. 10(a).

With these considerations in mind, we find that the relationship between the preliminary reports of STJs and the final, reviewable "decisions" of the Tax Court bears striking resemblance to the relationship between reports of "divisions" of the Tax Court and final decisions of the Tax Court itself. A "division" is a subset of the Tax Court (often a single judge) that is designated to hear a single case and is empowered to make determinations with respect to disputes before the Tax Court. 26 U.S.C. §§ 7444(c), 7460(a). Under § 7460, the division's decision generally becomes the decision of the Tax Court, but the Tax Court retains the power to review the division's decision and render its own. Those preliminary recommendations of the division which do not become part of the final decision of the Tax Court also do not become part of the record for any additional future review. *Id.* § 7460(b) ("The report of a division shall not be a part of the record in any case in which the chief judge directs that such report shall be reviewed by the Tax Court.").

Thus, the two circuits to have interpreted § 7460 have ruled that a division's preliminary report is not part of the appellate record and not available for review by a federal appeals court once the Tax Court has undertaken an internal review. *See Estate of Varian v. Comm'r*, 396 F.2d 753, 755 n.2 (9th Cir. 1968); *Heim v. Comm'r*, 251 F.2d 44, 48 (8th Cir. 1958). The Ninth Circuit noted a congressional intent in § 7460 to preclude a two-tier appellate relationship between the division and the full court and determined that such a mandate did not offend the court's notions of fundamental fairness. *Varian*, 396 F.2d at 755 n.2.

Given the similarities between these two relationships, we are led to the same conclusion that the Ninth Circuit reached in *Varian*: there is no two-tier appellate relationship between STJs and the Tax Court. Instead, STJ reports are treated by the Tax Court as preliminary findings only and, in

accordance with applicable rules and statutes, are not required to be made part of the record on appeal.

The dissent takes issue with this comparison, noting that divisions are comprised of one or more Tax Court judges, who are all presidentially appointed and serve a fifteen-year, statutorily mandated term of office from which they can be removed only for "inefficiency, neglect of duty, or malfeasance in office but for no other cause." 26 U.S.C. § 7443(f). STJs, however, serve at the discretion of the Chief Judge and have no statutorily mandated term of office. *Id.* § 7443A. If Tax Court Rule 183 provides for a quasi-collaborative process, the dissent fears this distinction between the participants impairs the judicial independence of the STJ. As a result, the dissent questions whether an STJ can participate meaningfully in this internal deliberative process. *See post* at 87.

We respectfully disagree. We are hesitant to suggest that members of the Tax Court would either expressly coerce or by nature of their office exert undue influence over an STJ. Nor will we discredit an STJ's express statement that the final Tax Court opinion "agrees with" his own based solely on this observed distinction.

This procedure, while admittedly unusual vis a vis typical judicial procedure, does not offend our notions of fundamental fairness. *See Varian*, 396 F.2d at 755. In this respect, we agree with the dissent's conclusion that due process neither requires the Tax Court to be constrained by a formal degree of deference to the STJ nor requires the Tax Court to rehear witnesses whether or not it ultimately reverses the STJ's findings. *See post* at 89-94 (discussing *United States v. Raddatz*, 447 U.S. 667 (1980) and *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 492-94 (1951)). Although *dictum* in the Supreme Court's decision in *Raddatz* suggests that "serious questions" may arise from a district court's reversal of a magistrate judge's credibility findings without the opportunity to personally see or hear the witnesses, *see* 447 U.S. at

681 n.7, that observation was made within the context of a criminal appeal. In a civil tax proceeding, a party's interests are more akin to those at stake in a typical administrative adjudication, and we agree with the dissent that the risk of erroneous deprivation in a civil proceeding is neither "as high, nor the costs as great, as would be the case in a criminal milieu." *See post* at 93 (discussing Tax Court Rule 183 within the procedural-due-process framework established by *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976)). Moreover, we agree that the "only fully responsive remedy" to Kanter's complaint would prove unworkable, as it would require the enormous burden and prohibitive cost of rehearing witnesses, which would ultimately prove to add little value given the continued input that the STJ retains under Tax Court Rule 183's purportedly quasi-collaborative process. *See post* at 883-884.

But the recognition that little value would be added to the process given the STJ's continued involvement – signified by his adoption of the statement that the final Tax Court opinion reflects his own opinion – is ultimately why we take issue with the dissent's conclusion that our review of the Tax Court's opinion is unconstitutionally impaired by this procedure. The conclusion rests on the premise that STJs do not enjoy an equal voice in this purportedly quasi-collaborative process. *See post* at 886-887. As discussed above, we reject this premise. In as much as the final Tax Court opinion purports to agree with and adopt the opinion of the STJ, we therefore believe that the final opinion reflects the true legal opinions and findings of the STJ. Any differing preliminary recommendations – if they ever existed – would no longer be constitutionally relevant because the STJ has abandoned them. Should he feel otherwise, we would expect him – or the Tax Court – to say so.

As the Eleventh Circuit recently noted, "there is nothing unusual about judges conferring with one another about cases

assigned to them." *Ballard*, 321 F.3d at 1043. If Tax Court Rule 183 in fact provides the opportunity for STJs and Tax Court judges to conference regarding the STJ's preliminary findings, then we have every reason to believe that Tax Court judges would duly regard the input of the STJ and that he, in turn, would participate meaningfully in the exchange. Like the Ninth and the Eleventh Circuits, we too are loath to interfere with another court's deliberative process. *See id.*

In any event, the issue is academic since the Tax Court's opinion in this case purports to "agree with and adopt" Special Trial Judge Couvillion's opinion. We will take the Tax Court at its word and, thus, move on to a discussion on the merits of Kanter's appeal.

II. Fraud

A. Facts

The bulk of the Tax Court's opinion involves its determination that certain income tax underpayments were made with fraudulent intent. The facts surrounding the fraud issue are the most complex of all and will be described as succinctly as possible.

The Tax Court's decision tells a story of Kanter and two business associates – Robert Lisle and Claude Ballard. Lisle and Ballard worked in real estate, principally as managers in the real estate division of Prudential Insurance Company, where they had significant authority and influence over the conduct of Prudential's business. Kanter, Lisle, and Ballard concocted a plan whereby they would use Lisle and Ballard's positions along with Kanter's legal skills to collect and hide payments from people who wanted to do real estate business with Prudential.[7]

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[7] As the Tax Court opinion notes, there were additional sets of transactions that involved only Lisle and Kanter during Lisle's

The Tax Court focused on five individuals (referred to collectively as the Five) who paid Kanter, Lisle, and Ballard for their influence.[8] For the Five, Lisle and Ballard would help secure business opportunities with Prudential, and in return the Five made payments, including cash and partnership interests, to Kanter.

It was at this point that the IRS became interested. According to the Commissioner these payments were diverted (the Commissioner and Tax Court use the more highly charged word "laundered") to entities created by Kanter or someone acting at Kanter's direction. The dominant method was to divert payments to a Kanter-controlled corporation called Investment Research Associates, Ltd (IRA).[9]

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post-Prudential career at Traveler's Insurance Company as well as transactions involving Kanter alone. *IRA*, 78 T.C.M. (CCH) at 970-71. These transactions followed the same pattern detailed here where Kanter used his influence to secure business opportunities for individuals in return for compensation that was then diverted through a series of entities in order to disguise the origin of the funds and avoid income tax liability. For the sake of simplicity we will refer only to the transactions involving Prudential and the Five as representative of all of the transactions detailed by the Tax Court.

[8] The Five were J.D. Weaver, Bruce Frey, William Schaffel, Kenneth Schnitzer, and John Eulich. The details of the transactions involving the Five are in the Tax Court opinion at 78 T.C.M. (CCH) at 976-1019.

[9] IRA was originally incorporated in 1974 in Delaware as Cedilla Co. It was intended as a vehicle for making investments. Cedilla changed its name to Investment Research Associates in 1979. IRA owned as relevant subsidiaries, at various times, Carlco, TMT and BWK, Inc. IRA conducted no business and had no employees other than bookkeepers and paid virtually no amount in salaries.

The payments to IRA were deposited in the accounts IRA kept with another Kanter-controlled entity called the Administration Company. The Administration Co. was exactly what its name indicates: a company that administered the records and funds of its clients. It maintained books and records for its clients, and often prepared client tax returns. Additionally, it administered client funds, collecting receivables and paying bills. Money for clients was kept in pooled bank accounts listed under Administration Co.'s name. Two of these accounts were called the Special E account and the TACI Special Account. Client funds were pooled in order to get the higher rate of return on aggregated funds and to avoid a multiplicity of account maintenance charges on many, smaller client bank accounts kept in the clients' individual names. Administration Co. itself (and not the bank where the accounts were kept) tracked individual client balances within the pooled accounts on its internal records for each client. IRA and many of its subsidiaries were clients of Administration Co.[10] In fact, it does not appear that Administration Co. had any significant clients not directly associated with (or controlled by) Kanter.

The payments by the Five to IRA that were deposited in the accounts of the Administration Co. were commingled with other non-Five-related funds of IRA as well as the funds of other Administration Co. clients. This commingling and the inadequate record keeping of Administration Co. made it difficult to track or account for the payments from the Five.

It was IRA – and not Kanter, Lisle, or Ballard – that reported the income from the Five's payments on its tax return

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[10] In 1988, the Administration Co. filed for bankruptcy. Concurrently, a company called Principal Services was organized, and took over many of Administration Co.'s clients, operating with the same purposes and in the same way as had Administration Co.

(where it was off-set by aggregated losses). Subsequently, IRA distributed the income into subsidiary "sham" corporations, BWK, Carlco, and TMT, controlled by Kanter, Lisle, and Ballard, respectively, in a 10/45/45 ratio, respectively, that represented the division of the payments allegedly agreed to by Kanter, Lisle, and Ballard.[11] These sham corporations were used, in effect, as the personal bank accounts of Kanter, Lisle, and Ballard, and these men could withdraw or use the funds contained in them at their leisure.[12] The funds withdrawn were never repaid and were eventually written off as bad debts. Alternatively, the controlled corporations' funds were used to fund the personal expenditures of Kanter, Lisle, and Ballard, as well as their families.

Kanter, on the other hand, argues that the payments to the corporations were merely investments by the entities, "ceded" to them by Kanter. The underlying scheme of securing business opportunities for the Five interested individuals in return for payments to Kanter (through Kanter entities) is disputed in its entirety by Kanter.

The Commissioner argued, and the Tax Court agreed, that this income was properly taxable to the individuals, and

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[11] Carlco, TMT, and BWK were "shelf" corporations formed by Kanter in 1982. In 1983, they became active, and IRA acquired 100% of the common stock of each. In 1984, each corporation issued shares of preferred stock. Carlco issued its preferred shares to the Christie Trust, a trust established by Kanter for the benefit of Lisle's family. TMT's preferred shares were issued to the Orient Trust, established by Kanter for the benefit of Ballard's family. BWK's preferred shares were issued to the BK Children's Trust, established for the benefit of Kanter's family. As part of the scheme, Lisle controlled Carlco's investment decisions, Ballard controlled TMT's and Kanter controlled BWK's.

[12] The actions summarized in these few sentences took place over many years.

a deficiency was assessed. The Tax Court held that the diversion of these funds from the individuals to the sham corporations was undertaken with the fraudulent intent to evade the payment of taxes. According to the Tax Court, this arrangement not only disguised income earned by the individuals, but also hid their activities from Prudential.

In the Tax Court, Kanter presented an impressive list of witnesses associated with Kanter, Lisle, Ballard, the Five, and the various relevant entities – all of whom expressly denied that the Five paid "kickbacks" to Kanter for steering business the Five's way. But the Tax Court found that these witnesses had testified that the Five had, in fact, entered into payment arrangements with Kanter, Lisle, and Ballard in exchange for their influence in obtaining business. *IRA*, 78 T.C.M. (CCH) at 1065. This testimony established that Kanter had not reported income on which he was taxable and had therefore underpaid his federal-income-tax obligations. The Tax Court found that these underpayments were undertaken with intent to evade taxes based on, *inter alia*, the following factors: the lack of credibility of Kanter's testimony; Kanter's legal education and experience indicating an awareness of his obligation to report income accurately and pay taxes; Kanter's substantial underreporting of income for many years; Kanter's creation of a complex laundering network of sham corporations and other entities that made it difficult to trace the flow of funds; Kanter's lack of cooperation with the IRS – namely, the withholding of documents and the destruction of documents subject to summonses; Kanter's commingling of "kickback" monies with other monies in the Administration Co.'s accounts; Kanter's movement of monies through conduits that had no legitimate business purpose showing an intent to disguise sources of funds; Kanter's reporting of his personal income on the tax returns of IRA in order to create the appearance that income was earned by IRA; and Kanter's use of phony loans to disguise distribu-

tions to himself, later written off as bad debts. *IRA*, 78 T.C.M. (CCH) at 1083-85.

B. Analysis

A finding of fraud by the Tax Court is a factual finding that we review for clear error. *Toushin v. Comm'r*, 223 F.3d 642, 647 (7th Cir. 2000). As with all findings of fact of the Tax Court, we must view the evidence in the light most favorable to the Tax Court's findings and reverse only if we are left with the definite and firm conviction that a mistake has been made. *Pittman*, 100 F.3d at 1312-13.

To establish fraud, the Commissioner must prove by clear and convincing evidence that Kanter's underpayment of taxes was done with intent to evade taxes that he knew or believed were owed. *Toushin*, 223 F.3d at 647; *Pittman*, 100 F.3d at 1319. Fraud may be proven through circumstantial evidence. *Pittman*, 100 F.3d at 1319. There are a variety of commonly recognized indicia of fraud, "such as keeping a double set of books, making false entries or alterations, [using] false invoices or documents, [destroying] books or records, [concealing] assets or covering up sources of income, handling * * * one's affairs to avoid making the records usual in transactions of the kind, and [undertaking] any conduct, the likely effect of which would be to mislead or to conceal." *Spies v. United States*, 317 U.S. 492, 499 (1943). Additionally, fraud can be shown by significant and repeated understatement of income, *Pittman*, 100 F.3d at 1320, by a lack of cooperation with investigating agents, *Korecky v. Comm'r*, 781 F.2d 1566, 1568-69 (11th Cir. 1986); *Zell v. Comm'r*, 763 F.2d 1139, 1146 (10th Cir. 1985), by destruction of records, *Powell v. Granquist*, 252 F.2d 56, 59 (9th Cir. 1958), or by considering the legal experience and education of the taxpayer, *Plunkett v. Comm'r*, 465 F.2d 299, 303 (7th Cir. 1972).

Kanter's principal argument is based on the representation he makes above concerning the STJ's report: Kanter and his witnesses *were* found credible, and his story was believed by the STJ. Therefore, there can be no finding of intent to defraud. It was, Kanter alleges, only the rejection of the STJ's findings by the Tax Court judge that led to the finding that Kanter was not credible and that the underpayment of taxes was accomplished with fraudulent intent. As discussed above, we refuse to credit Kanter's allegations in light of the Tax Court's statement that it "agrees with and adopts" the opinion of the STJ. Therefore, Kanter's principal argument is without merit. The Tax Court found that Kanter's testimony was not credible and also found significant circumstantial indicia of fraud. Kanter's arguments now do not demonstrate that this is clearly erroneous.

Kanter's remaining arguments are also meritless. He argues that it is a common estate planning technique to cede personal investments to family trusts and corporations. But he does nothing to undermine the considerable evidence cited by the Tax Court that demonstrates that the Five paid for Kanter, Lisle, and Ballard's help in securing business opportunities, and that those payments went through IRA to Carlco, TMT, and BWK for division of the proceeds in a 10/45/45 split. And inasmuch as this argument seeks to show a lack of fraudulent intent by attacking the existence of a deficiency, this argument was expressly waived by Kanter.

Additionally, Kanter argues that fraud was raised by the respondent late in the process by the Commissioner's amendment to his Answer, that none of the Commissioner's notices of deficiency indicated fraud and that IRS agents' reports had found no intent to defraud. While the Tax Court might have found this persuasive when, as the trier of fact, it considered the issue of fraud, this argument is unpersuasive at this stage. Kanter does not argue that the Commissioner's amendment was improperly allowed or otherwise defective.

Nor is the Commissioner's delayed amendment particularly probative of the sufficiency of the fraud evidence, given the difficulties facing the Commissioner in unraveling the relevant transactions during the time leading up to (and during) the trial.

Finally, Kanter's attacks on the circumstantial indicia of fraud are little more than efforts to recharacterize the evidence in a manner favorable to Kanter's version of events. But a review of the record in the light most favorable to the Tax Court's findings makes clear that it was not clear error to find significant indicia of fraud.

To review just a few of the relevant indicia: first and foremost, even Kanter concedes that he significantly underreported his income from the transactions with the Five over many years. (Pet. Br. at 33.)

Second, the money earned by Kanter through the transactions with the Five was diverted to IRA and commingled with other monies, where the funds were reported as income earned by IRA, before ultimately becoming available to Kanter personally – a complicated money trail that made it difficult to trace the flow of the funds and gave the appearance that the money had been earned by IRA.

Third, there was evidence that Kanter and those acting at his behest did not cooperate with investigating agents and even destroyed records that the IRS had requested formally through its summons power. *See* 26 U.S.C. § 7602. James Lunk, an IRS Case Manager, was asked during his testimony at trial what records Kanter and his representatives had provided voluntarily, to which he responded, "Generally they were records that really wouldn't do us a lot of good in the examination in terms of really getting at the type of information we needed to examine the transactions that we were most interested in." (Tr. at 1055-56.) IRS Agent Paul Dion testified similarly:

> I have some very direct recollection[s] of the meeting, because it was the first time I met Mr. Kanter. And at the very beginning of the meeting, we discussed some – had a very nice conversation relating to very general type[s] of topics. I remember art was one of them, and a few other generalities. And as soon as we started discussing the required documentation, it was almost as if a different person appeared. And that person became, I guess, very demonstrative in terms of not wanting to provide us with the information that we asked for; basically saying that he was going to frame the issue and not us.

(Tr. at 831-32.) The Commissioner had to seek the assistance of the district court in order to enforce summonses against Kanter seeking documents relevant to the present case. The district court, in two separate rulings, indicated that Kanter had not cooperated and that documents had been destroyed even after the IRS summonses for those documents had been issued.[13] The court stated that

> [Solomon] Weisgal testified that since [receiving a summons to compel production of documents], some of the BK documents, including summoned documents relating to the Kanters, had been turned over to the Administration Company and that some have been discarded as part of a three-year record retention and discard policy * * *. [Linda]

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[13] Kanter's argument that the documents were destroyed according to a standard document retention policy is unpersuasive. The existence of a document retention policy, which appears to have been enforced inconsistently, cannot justify the destruction of documents that were already subject to an IRS summons. Further, we agree with the Tax Court and believe that it is clear from the record that Linda Gallenberger (Kanter's accountant and Administration Co. employee) and Solomon Weisgal (Kanter's associate and trustee/officer for various Kanter entities) acted at the direction of Kanter.

> Gallenberger testified that she disposed of some documents [related to Kanter] after receipt of the IRS summons.

United States v. Administration Co., 74 A.F.T.R.2d 94-5252, 1994 WL 240518, at *2 (N.D. Ill. May 31, 1994). The district court went on to note that

> The facts are that the Kanters first promised to produce the documents sought from [entities involved in the present case] and then, in early February 1994, notified government counsel that the Entities were third-parties over whom they had no control. The eleventh-hour change of position by the Kanters is indicative of bad faith on the part of the Kanters.

Id. at *3. Less than a month later, the same judge held Gallenberger in contempt for a continuing failure to comply fully with IRS summonses. *United States v. Administration Co.*, 74 A.F.T.R.2d 94-5256, 1994 WL 285064, at *2 (N.D. Ill. June 23, 1994) ("Gallenberger misconceives her duty to use all reasonable efforts to comply with the summonses. A half-hearted request and cursory further search are insufficient.") (internal quotations and citations omitted).

These and the other indicia cited by the Tax Court, when considered in a light favorable to the Tax Court's findings, paint a clear and convincing picture of an intent by Kanter to evade the payment of taxes he knew or believed that he owed. It was not clearly erroneous for the Tax Court to find that Kanter's underpayment of taxes involved fraud.

III. Bea Ritch Trusts

A. Facts

The Bea Ritch Trusts (BRT) are a group of twenty-five trusts established in 1969 under one trust document. The trust document named Beatrice Ritch, Kanter's mother, as the grantor of BRT, Kanter's friend and business associate Solomon Weisgal as the trustee and the members of Kanter's

family as the beneficiaries. According to the trust document, Beatrice Ritch funded each of the separate BRT trusts with a $100 check. No evidence (beyond the trust document itself) was presented to substantiate that this actually happened. Kanter himself was originally named as a beneficiary of twenty-four of the twenty-five trusts and he alone was granted a power of appointment over the beneficial interest of BRT. Kanter allegedly renounced his interest in BRT in 1971, 1977, and 1978, thereby purportedly eliminating his power of appointment over BRT. At sometime during or before 1987, however, sixty new beneficiaries were added to BRT.

Before 1987, Kanter borrowed money from BRT, and as of January 1, 1987, Kanter still owed the trust $287,030. This debt does not appear to have been secured, nor is there any indication in the record that a reasonable interest rate (if any) was charged on the loans.

In the early 1970s Kanter participated in business ventures in Long Island, New York, involving the then nascent cable television industry. He and other members of his law firm helped an entity that eventually became Cablevision Co. raise funds, secure financing and find investors for its cable business. In return, Kanter (along with others) was to receive interests in partnerships that themselves owned interests in Cablevision.[14] Kanter arranged to have BRT receive the Cablevision partnership interests to which he was entitled – in

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[14] We speak in generalities in order to avoid further confusing the situation by expanding the alphabet soup of partnership and trust abbreviations, whose exact identities are not necessary to explain the factual background of this issue. The Tax Court's opinion fully identifies all the relevant entities. *See IRA*, 78 T.C.M. (CCH) at 1093-1100. We will simply refer to the partnership interests transferred to IRA for Kanter's services to Cablevision as the Cablevision partnership interests.

essence he contributed the Cablevision partnership interests to BRT. The Tax Court found that the contribution of Kanter's Cablevision partnership interests (along with other income and assets) to BRT was the principal source of funding for BRT. Kanter, therefore, was the true grantor of BRT. *IRA*, 78 T.C.M. (CCH) at 1098-99.

In 1987, BRT reported capital gains of $2,033,368 for the fiscal year ending September 30, 1987, from the sale of the Cablevision partnership interests owned by BRT.[15] Because Kanter was the true grantor of BRT and because he had a power of appointment to name beneficiaries of BRT, the Commissioner assessed a deficiency for the year 1987 against Kanter with respect to BRT's income from the Cablevision sale. At trial, the evidence made clear that the income at issue had been earned during the calender year 1986, and the Commissioner sought to amend his pleadings and reallocate the BRT deficiency from 1987 to 1986. The Tax Court allowed the amendment, and denied Kanter's request to shift the burden of proof to the Commissioner for having raised a "new matter." *See* Tax Court Rule 142(a)(1).

The Tax Court found that Kanter had failed to prove that he did not fund BRT and, despite his three renunciations of any beneficial interest in BRT, that he had not appointed the 60 new beneficiaries. As a result, the Tax Court held Kanter liable for tax on BRT's income for 1986 and 1987 under the IRC's grantor trust provisions. 26 U.S.C. §§ 671, 674. The Tax Court also found that, in the alternative, Kanter's borrowing of trust funds made him taxable on BRT's income. *See* 26 U.S.C. § 675(3).

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[15] The partnerships in which BRT was a partner sold their respective interests in Cablevision itself, triggering a capital gain to the partnerships that then flowed-through to BRT. *See IRA*, 78 T.C.M. (CCH) at 1093.

B. Analysis

1. Was the allowance of the amendment proper?

Kanter's first argument concerns the Tax Court's allowance of an amendment of the pleadings to conform to the proof that the alleged deficiency relating to BRT applied to 1986 rather than to 1987. Kanter argues that it was error to allow this amendment at all, and that, once allowed, the Tax Court further erred by not treating this as a "new matter" under Tax Court Rule 142(a), which would have shifted the burden of proof on the issue to the Commissioner.

The decision to allow or deny an amendment of the pleadings under Tax Court Rule 41 is reviewed for abuse of discretion. *See Estate of Ashman v. Comm'r*, 231 F.3d 541, 542 n.2 (9th Cir. 2000); *LeFever v. Comm'r*, 100 F.3d 778, 786 (10th Cir. 1996); *Braude v. Comm'r*, 808 F.2d 1037, 1039 (4th Cir. 1986). It was not an abuse of discretion for the Tax Court to allow the amendment of the Commissioner's pleadings to reallocate the BRT deficiency to 1986. Kanter was on notice as to the specific partnership income of BRT that was the subject of the assessed deficiency. (Tr. at 4483-86.) There was no prejudice to Kanter in the adjustment of the date, and he had a fair opportunity to defend with respect to the amended claim. In fact, it was Kanter, and not the government, who elicited the testimony (from Kanter's accountant, Gallenberger) that revealed the timing error and prompted the government's request for amendment.[16] The

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[16] A fair reading of the trial transcript is that Kanter's strategy regarding the BRT income was from the beginning to demonstrate that the income in question had been earned in 1986, not 1987, and to try to shift the burden of proof to the Commissioner in precisely the manner argued here. (Tr. at 4455-4501.) With Kanter's clear advance knowledge of the calender mistake and his apparent strategic decision regarding that mistake, we find it hard to believe Kanter when he says this "was not an issue that Kanter was pre-

government apparently did not realize its error until Kanter pointed it out at trial. Further, Kanter points to no additional evidence that he was prevented from introducing by virtue of the late amendment. The amendment of the pleadings to conform to the evidence was proper.

2. Should the amendment have shifted the burden of proof?

Kanter argues next that the amendment to the pleadings was a new matter that shifted the burden of proof on this issue to the Commissioner. *See* Tax Court Rule 142(a)(1) ("The burden of proof shall be upon the petitioner, except * * * that, in respect of any new matter, * * * it shall be upon the respondent."). The distribution of burdens is a question of law that we review *de novo*. This argument fails as well. The Commissioner is allowed the latitude to amend his pleadings and even adopt entirely new *theories* supporting assessed deficiencies without triggering Rule 142's shift in burden, so long as the new theory is not inconsistent with the original allegation, does not require new evidence in its support, nor increases the amount of the deficiency. *See, e.g.*, *Friedman v. Comm'r*, 216 F.3d 537, 543 (6th Cir. 2000) ("A new position taken by Commissioner is not necessarily a 'new matter' if it merely clarifies or develops Commissioner's original determination without requiring the presentation of different evidence, being inconsistent with Commissioner's original determination, or increasing the amount of the deficiency."); *Abatti v. Comm'r*, 644 F.2d 1385, 1390 (9th Cir. 1981) (same); *Achiro v. Comm'r*, 77 T.C. 881, 890 (1981) (same).

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pared to defend at trial" – except inasmuch as this statement may reflect Kanter's belief at trial that a shifting of the burden of proof to the Commissioner would obviate any need to mount a substantive rebuttal defense.

The problem for Kanter is that the Commissioner's amendment did not offer a new theory for the alleged deficiency. The theory under which the Commissioner proceeded at all times was that specific transactions produced taxable income that was reported by BRT but which was properly taxable to Kanter by virtue of the grantor trust provisions of the tax code.[17] The case relied upon by Kanter here supports our conclusion. *Achiro* involved an amendment under which the Commissioner alleged for the first time that a deduction was improper under a section of the tax code completely different from the section originally argued. 77 T.C. at 889-90; *see also Shea v. Comm'r*, 112 T.C. 183, 190-92 (1999). The Commissioner's amendment here presented a much more modest change, more akin to a clarification of the original allegation. Nor is Kanter correct when he alleges that the amendment increased the assessed deficiency. The stated deficiency remained constant, and involved the same income from the same transactions, but was re-allocated from one disputed year to another disputed year to correct a calender error that did not prejudice Kanter's case.[18] The Com-

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[17] The Commissioner appears to be offering to split the baby with respect to the burden of proof issue by conceding that he bears the burden to prove that BRT actually had taxable income in the form of capital gains in 1986, but claiming he has met that burden. There can be no serious dispute that the monies in question were reported as earned in 1986 by BRT. It was Kanter's own accountant, Gallenberger, who, on redirect by Kanter, provided the testimony with respect to this fact. (Tr. at 4455-4501.) The only substantive issue in dispute is Kanter's status as grantor and owner of BRT under the IRC's grantor trust provisions, a theory unaffected by the amendment.

[18] This should obviously not be read to preclude the possibility that an amendment of the Commissioner's pleadings to shift an assessed deficiency from one year to another would result in a shifting of the burden under Rule 142(a)(1). But where, as here, the

missioner did not propose additional income nor require Kanter to defend against a larger deficiency than had been assessed before the amendment. Therefore, it is incorrect to claim that the amendment resulted in "an entirely *new* and *increased* deficiency *in a different year.*" (Pet. Br. at 46 (emphasis in original).) The Tax Court was correct in determining that the amendment did not shift the burden of proof to the Commissioner.

3. Kanter was the grantor of BRT

Although Kanter argues principally that the Commissioner should have borne the burden of proving that Kanter was the grantor and owner of BRT, and that the Commissioner could not meet that burden, Kanter maintains that, regardless of burden, he is not taxable on BRT's income under the IRC's grantor trust provisions. A finding of grantor status is a factual finding that we review for clear error. *Scott v. Comm'r*, 226 F.3d 871, 874 (7th Cir. 2000). Kanter has failed to show that the Tax Court's decision was clearly erroneous.

Despite the trust document's showing that Beatrice Ritch was the grantor of BRT, the familiar principle of substance over form views as the true grantor the one who principally funded the trusts. *Schulz v. Comm'r*, 686 F.2d 490, 496 (7th Cir. 1982); *United States v. Buttorff*, 761 F.2d 1056, 1060-61 (5th Cir. 1985). In *Schulz*, for example, the petitioner's wife was considered the grantor of a family trust because both the Commissioner and this court disregarded the conveyance of the wife's assets, which were subsequently used to fund the trust in question, to the petitioner. 686 F.2d at 496. The wife,

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amendment results from a good faith error in the timing of when specific income was earned from specific transactions and does not involve any change in the underlying theory of the deficiency, there is no shifting of the burden of proof to the Commissioner.

in substance, provided the funds for the trust, and the form of the funding, by routing the funds through the petitioner, was ignored. Similarly, although Kanter was not listed in the trust document as a grantor, and, even if Beatrice Ritch actually did contribute $100 towards the funding of each BRT trust, there is evidence that Kanter contributed to BRT income and assets he earned, to substantially fund the twenty-five trusts.

The Tax Court found that Kanter transferred to BRT income and assets associated with his services in the Cablevision transactions as well as others. *IRA*, 78 T.C.M. (CCH) at 1098. Kanter provided no evidence (other than the trust document itself) to show that Beatrice Ritch actually funded the trusts nor any evidence to show from whence the substantial assets owned by BRT originated. Kanter's assertion that he merely ceded investment opportunities in Cablevision to BRT does nothing to undermine the Tax Court's findings and, further, depends on his credibility, which the court found to be lacking. Because Kanter was the principal source of the funding of BRT, he is deemed a grantor of BRT. *See* 26 C.F.R. § 1.671-2(e)(1) ("[A] grantor includes any person to the extent such person either creates a trust, or directly or indirectly makes a gratuitous transfer * * * of property to a trust * * *. If a person creates or funds a trust on behalf of another person, both persons are treated as grantors of the trust.").

Kanter argues that the Tax Court's finding that he was the grantor is directly contrary to an Illinois trial court decision, in which the Cook County Circuit Court determined that the Cablevision partnership interests did not constitute property of Kanter's law firm because they did not result from payment of fees for legal services. *Statland v. Levenfeld*, No. 84 CH 6494 (Ill. Cir. Ct., Ch. Jan. 28, 1988). Kanter argues that (a) the state court ruling stands for the proposition that the Cablevision partnership interests were not in payment for *any* services (not just legal services) but were rather investments

and (b) the state court ruling is determinative and binding on the matter. Kanter overstates the holding of the cited case. The case involved a former law partner of Kanter, who alleged that the Cablevision partnership interests were the property of the partnership because they were provided in payment for legal services. The Illinois court disagreed and held that the Cablevision partnership interests were not the product of legal fees paid to Kanter's law firm. The court did not hold, however, that the Cablevision partnership interests were not in payment of fees for services furnished by individual law firm partners in securing financing and investors for Cablevision, which is what the Commissioner alleges here. The trial court did, at various times, refer to the Cablevision partnership interests as individual investments, but it also spoke of the activities of Kanter and his partners in working to obtain financing and investors for Cablevision. None of these *dicta* contradicts the position of the Commissioner nor renders the factual findings of the Tax Court clearly erroneous.

4. Kanter was the substantial owner of BRT

Generally, if a grantor of a trust has the power to dispose of the beneficial enjoyment of that trust through a power of appointment, then the grantor is treated as the owner of the trust and the income of the trust must be included in the income of the grantor. 26 U.S.C. §§ 671, 674(a); 26 C.F.R. § 1.674(a)-1. Kanter argues that he three times renounced his beneficial interest in BRT and, by those renunciations, lost the power of appointment that he had under the trust document. But the Tax Court notes that, after the third of Kanter's renunciations, sixty new beneficiaries were added to BRT.[19] Kanter was the only person who ever had the power

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[19] The new beneficiaries were all trusts – named and numbered variations of "JSK Trust." *IRA*, 78 T.C.M. (CCH) at 1094-95.

under the trust document to appoint new beneficiaries. The most logical inference (which the Tax Court drew) is that Kanter himself appointed the new beneficiaries and that his earlier renunciations were shams. Kanter fails to rebut this. Kanter's only argument directly on this issue appears in his reply brief, in which he argues that the Tax Court improperly refused to reopen the record to admit evidence that Kanter's children were the grantors of the various JSK Trusts that had been added as beneficiaries of BRT.[20] (Reply Br. at 18.) This purported evidence would not be probative of the issue whether Kanter had exercised the power of appointment under BRT. The Tax Court's findings that Kanter was the grantor of BRT and that he held a power of appointment of beneficiaries of BRT were not clearly erroneous. Therefore, the Tax Court's finding that Kanter is taxable on BRT's income in 1986 (and 1987) is also not clearly erroneous.

As an alternative, the Tax Court also found that Kanter's borrowing from BRT without repayment and without adequate security subjected Kanter to liability for BRT's income. *See* 26 U.S.C. § 675(3) ("The grantor shall be treated as the owner of any portion of a trust in respect of which * * * [t]he grantor has directly or indirectly borrowed the corpus or income and has not completely repaid the loan, in-

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[20] A possible logical alternative argument *not* made by Kanter (because, we must assume, it is not valid) is that the appointments were made by Weisgal under some power he possessed as trustee. The Tax Court, the Commissioner and Kanter all spend significant time arguing whether Weisgal is or is not an independent and adverse trustee. An affirmative determination of that question would be necessary if Weisgal were to have appointed the sixty new beneficiaries or if Kanter were able to prove that he (Kanter) did not appoint them. Because we find that the Tax Court's determination that Kanter exercised a power of appointment was not clearly erroneous, we need not consider whether or not Weisgal was an independent and adverse trustee of BRT.

cluding any interest, before the beginning of the taxable year."). It appears undisputed that Kanter had borrowed money from BRT in a way that subjects him to liability under § 675(3), and that at the beginning of 1987 he still owed BRT $287,030. This would be sufficient for Kanter to incur liability for 1987.[21] There are, however, no findings by the Tax Court as to any amount Kanter owed to BRT as of January 1, 1986. Therefore, there could be no tax liability for Kanter in 1986 based on § 675(3). In the end this conclusion does not affect ultimate tax liability because under § 674 Kanter remains liable for both 1986 and 1987.

In conclusion, we affirm the Tax Court's determination that Kanter was the grantor of BRT in 1986 and 1987 and is taxable on BRT's income for those years.

IV. George Washington Painting

A. Facts

In 1980, Kanter was approached by Richard Feigen, a client, who wanted help in securing funding to buy a painting of George Washington located in England that Feigen believed to be by John Trumbull.[22] Kanter put Feigen in touch

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[21] The existence of these facts, however, would raise an additional issue, which we will not attempt to resolve today. Would we, as Kanter claims, need to analyze the amount of the loans in relation to the trust's income during the years the loans were made and from that determine what portion of the trust income from 1987 is attributable to Kanter? *See Bennett v. Comm'r*, 79 T.C. 470, 484-85 (1982). Or can we, as the Commissioner urges, merely consider the significant amount of the loans as indicative of Kanter's total control over BRT's income and therefore attribute all of the income for 1987 to Kanter? *See Benson v. Comm'r*, 76 T.C. 1040, 1047-48 (1981).

[22] John Trumbull was a painter of scenes and individuals from the time of the founding of the United States. He is, perhaps, most

with another client, Mr. Rappaport,[23] in Switzerland, who agreed to finance the purchase of the painting. The transaction closed. After the purchase, the painting was discovered not to be a Trumbull, and the seller agreed to rescind the sale. As a result of exchange rate and interest rate changes, Rappaport, who had advanced the funds, lost money. Rappaport wanted to be made whole, and when rebuffed, threatened to sue Feigen and Kanter for his claimed loss. Kanter, in convincing Feigen to reimburse Rappaport, agreed to provide $94,231 of his own funds. Kanter also paid $10,000 in legal fees incurred throughout the course of the transaction.

On his 1980 tax return, Kanter claimed the sum of $104,231 as a deduction on Schedule C, stating that his main business activity was "buying and selling paintings." The IRS disallowed the claimed loss. The Tax Court found, based on Kanter's testimony, that Kanter's main occupation was as an attorney and that he did not hold himself out as an art expert or art dealer. This made the claimed deduction unrecognizable under 26 U.S.C. § 162 as an ordinary and necessary business expense. Additionally, the Tax Court did not allow this deduction as a § 212 expense for production of income "because Kanter received no fees and no contract existed therefor, [and so] the expenditure did not bear a reasonable and proximate relationship to the production of income." *IRA*, 78 T.C.M. (CCH) at 1121. "[Kanter] merely served as an intermediary to introduce Feigan to another

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well known to the general public as the painter of the famous "Declaration of Independence" painting that dramatized (more accurately, fictionalized) the scene of the signing of the Declaration of Independence, and that is familiar to almost every American schoolchild from its reprinting in countless American History textbooks.

[23] Neither the parties' briefs nor the trial transcript reveal Mr. Rappaport's first name.

friend, Rappaport. There was no written contract between Feigan and Kanter for the sharing of profits." *Id.*

B. Analysis

The Commissioner's determination that Kanter's expenses associated with the failed sale of the Washington painting were not legitimate deductions under 26 U.S.C. §§ 162 and 212 is a finding of fact that we review for clear error. *Reynolds v. Comm'r*, 296 F.3d 607, 615 (7th Cir. 2002); *Buelow v. Comm'r*, 970 F.2d 412, 415 (7th Cir. 1992).

The Tax Court found, essentially, that Kanter could not deduct the expenses under §§ 162 and 212 because Kanter's business was the practice of law, not art, and there was no evidence that Kanter had an agreement with Feigen to receive fees or share profits from the purchase and planned resale of the painting. The Tax Court simply did not believe the "self-serving and uncorroborated" testimony of Kanter. *IRA*, 78 T.C.M. (CCH) at 1121. Given the totality of the Tax Court's findings that Kanter systematically engaged in extensive (non-law related) business dealings whereby he "entered into arrangements pursuant to which he would use his * * * contacts * * * to assist individuals * * * in obtaining business opportunities or in raising capital for business ventures[,]" we find it implausible for the Tax Court to conclude that Kanter was not engaged in such dealings when he helped Feigen secure financing from Rappaport. *IRA*, 78 T.C.M. (CCH) at 970.

Without excessively detailing the transactions relating to the Five that we summarized in Part II, we note that the Tax Court's opinion went to considerable lengths to confirm deficiencies against Kanter based on a characterization of Kanter's "business" as ranging far beyond the simple practice of law. In each of the transactions involving the Five, the foundation for the Tax Court's determination that Kanter consistently understated his income was its findings that time

after time Kanter provided non-legal business services in facilitating business opportunities for the Five with Prudential, and that he was paid handsomely for that facilitation. It is difficult for us to read the first few hundred pages of the Tax Court's opinion and not be left with the distinct impression that the Tax Court believes Kanter was involved in this business "activity with continuity and regularity and * * * [his] primary purpose for engaging in the activity [was] for income or profit." *Comm'r v. Groetzinger*, 480 U.S. 23, 35 (1987). At the very least, Kanter has shown a distinct proclivity to seek income and profit through activities similar to the failed sale of the painting.

Determining whether an activity was engaged in for profit requires an examination of the relevant factors outlined in Treasury Regulation 1.183-2. *See* 26 C.F.R. § 1.183-2; *Burger v. Comm'r*, 809 F.2d 355, 358 (7th Cir. 1987). The nine factors for determining whether Kanter's involvement in the sale of the George Washington painting was carried on for profit include: (1) the manner in which the taxpayer carries on the activity; (2) the expertise of the taxpayer; (3) the time and effort expended by the taxpayer in carrying on the activity; (4) the expectation that assets used in the activity may appreciate in value; (5) the success of the taxpayer in carrying on other similar or dissimilar activities; (6) the taxpayer's history of income or losses with respect to the activity; (7) the amount of occasional profits, if any, which are earned; (8) the financial status of the taxpayer; and (9) elements of personal recreation or pleasure in carrying on the activity. 26 C.F.R. § 1.183-2(b).

We can, based on Kanter's testimony and considering the Tax Court's other findings, construct a highly probable scenario under which Kanter was to find financing for Feigen's purchase in exchange for part of the anticipated profits. Under factor (1), this manner of doing business, while not well documented, is consistent with the method pursued in other

transactions detailed by the Tax Court. Under factor (2), Kanter's apparent expertise in facilitating financing transactions and putting people together for deals in order to generate income was so evident to the Tax Court that it found him liable for large underpayments of income tax. Additionally, Kanter has indicated that the art project was attractive because of Feigen's expertise in generating sufficient publicity and excitement about artwork to likely increase the resale price, thus satisfying factor (4). (Tr. at 4416-30.) Regarding factor (5), Kanter's obvious success in other facilitation-of-business ventures was what landed him in trouble with the Commissioner in the first place. An appealing tale of the Washington painting scheme as a failed for-profit venture emerges from this evidence. In fact, while there is significant evidence that Kanter undertook similar, though not identical, transactions as the failed painting purchase for profit, there is no evidence that Kanter facilitated any other deals of this kind for personal reasons (i.e., gratuitously). And the Commissioner presents no evidence contradicting Kanter's version of events. In fact, by asserting that, in all of his other disputed transactions in which income was produced, Kanter had participated in the manner alleged here and with the kind of profit motive he alleges here, but arguing that in this *single* transaction, where losses were generated, Kanter participated for only personal reasons, the Commissioner appears to want to have his cake and eat it too.

There are certain difficulties in reversing the Tax Court here. We would have to reverse the Tax Court's credibility finding on the matter. In that connection, neither Feigen's testimony, nor Rappaport's testimony, nor any piece of specific evidence exists in the record to support Kanter's testimony. And we have found elsewhere that, while a taxpayer's uncontradicted testimony was sufficient to demonstrate that the Commissioner's determination was erroneous, the Tax Court can disregard that testimony if it is not credible. *Lerch*

v. Comm'r, 877 F.2d 624, 631 (7th Cir. 1989). The Tax Court did not here believe Kanter's claim of a profit motive. While finding Kanter not credible in this instance is consistent with the Tax Court's refusal to find him credible on other issues, it results in a completely inconsistent and implausible factual scenario – Kanter's incurring more than $100,000 in expenses gratuitously to facilitate a business transaction where huge potential profits lie. But without any indication why this transaction is unique among all the other Kanter activities, we think the Tax Court was clearly erroneous in rejecting Kanter's claim that he was pursuing commercial objectives here as elsewhere.

In conclusion, we find that there must have been a profit motive in Kanter's involvement in the aborted purchase of the George Washington painting; the Tax Court's finding to the contrary is clearly erroneous and we reverse. Kanter's deduction for the $104,231 of expenses incurred in facilitating the failed sale of the George Washington painting is allowed.

V. Bank Deposit Analysis

A. Facts

In examining Kanter's 1982 tax return, the IRS determined that inadequately documented deposits into three of Kanter's bank accounts during that year greatly exceeded the income Kanter reported on his federal tax return. Based on a comparison of the deposit amounts to Kanter's tax return for 1982, the Commissioner determined that Kanter had unreported gross income that year in an amount of $2,084,017, and issued an assessment of deficiency. After Kanter produced sufficient records documenting some of the deposits in question, the Commissioner reduced this deficiency to $1,303,207, which comprised the sum of four specific deposits:

DEPOSIT AMOUNT	PAYOR OR SOURCE
$787,129	The Holding Co. (THC)[24]
$40,000	Computer Placement Services, Inc. (CPS)[25]
$190,078	Administration Co. (Special E Account)
$286,000	Administration Co. (Special Account)

The Tax Court found that the Commissioner had produced sufficient evidence to create a presumption of correctness in the indicated deficiency. The bank deposit analysis method was a reasonable method of reconstructing income, and deposits from THC, CPS and the Administration Co. accounts often included taxable income. Therefore it was proper, the Tax Court ruled, for the Commissioner to determine gross income from an analysis of total deposits to Kanter's bank account minus any deposits properly excluded from income and to assess a deficiency for the excess of that income over the reported income. The Tax Court found that Kanter had not adequately documented that the four deposits in question were loans, and they were properly included in his gross income under the deposit analysis. Moreover, the Court did not find the testimony of Kanter's accountant, Gallenberger, credible on the issue.

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[24] THC was a Kanter entity incorporated in 1976. Its purpose, like that of IRA, was the making of investments. One of the relevant subsidiaries of THC was Zion Ventures, Inc. (Zion). *See infra* Part VI. The stock of THC was substantially owned by the BRT and Everglades Trusts 1-5 (Everglades Trusts), which were Kanter trusts whose income was attributable to Kanter via the IRC's grantor trust provisions, 26 U.S.C. §§ 671 *et seq.*

[25] The record does not indicate who holds legal or beneficial ownership of CPS.

B. Analysis

The Tax Court's determination that a taxpayer has unreported income is a finding of fact that we review for clear error. *Reynolds*, 296 F.3d at 612. The Commissioner's assessment of a deficiency is presumed correct, but can be overcome by rebuttal evidence presented by the taxpayer. *Pittman*, 100 F.3d at 1313.

Kanter has three arguments with respect to the deficiency determined by the bank deposit analysis: first, the change in the amount of the deficiency for 1982 under the bank deposit analysis constituted a "new matter" under Tax Court Rule 142 that required the burden of proof to shift to the Commissioner, and with that burden the Commissioner cannot prevail. Second, the lack of evidence on this issue made the deficiency a "naked assessment," and it was, therefore, improper to give the Commissioner's assessment of a deficiency the usual presumption of correctness. *See Weimerskirch v. Comm'r*, 596 F.2d 358, 360 (9th Cir. 1979) (finding no presumption of correctness when Commissioner's assessed deficiency lacks any reasonable foundation in the evidence). Finally, Kanter argues that the Tax Court clearly erred in finding a deficiency in light of the evidence presented. All of these arguments fail.

First, there is no merit in Kanter's contention that the Commissioner's reduction in the amount of deficiency assessed in 1982 under the bank deposit analysis is a new matter requiring a shift in the burden of proof. The Commissioner's concession that part of the original deficiency was properly excluded from Kanter's income is not a new theory, is not inconsistent with the original assessment of deficiency, does not require new or different evidence from Kanter and does not increase the assessed deficiency. *See* discussion *supra* Part III. The same theory of bank deposit analysis was being applied before and after the Commissioner's concessions, and the resulting deficiency was

reduced, not increased, when Kanter produced documentation demonstrating to the Commissioner's satisfaction that certain deposits were not income. The remaining, insufficiently documented deposits, therefore, do not constitute a new matter.

Nor can Kanter escape the presumption of correctness by relying on the "naked assessment" exception of *Weimerskirch*. "The general rule is that a presumption of correctness attaches to the Commissioner's deficiency determination; the taxpayer has the burden of disproving it. A narrow exception exists where the determination is arbitrary and erroneous or without rational foundation." *Pfluger v. Comm'r*, 840 F.2d 1379, 1382 (7th Cir. 1988) (citations omitted). It is not disputed that "before the Commissioner can rely on [the] presumption of correctness, the Commissioner must offer some substantive evidence showing that the taxpayer received income from the charged activity." *Weimerskirch*, 596 F.2d at 360. But the threshold for properly invoking the presumption is not as high as Kanter would have us believe, nor is the evidence presented by the Commissioner as thin as that presented in *Weimerskirch*.

In *Weimerskirch*, the Commissioner assessed a deficiency based on more than $24,000 of unreported income from the taxpayer's alleged sale of heroin. *Id.* at 359. The Commissioner, however, presented no evidence from which one could even *infer* that Weimerskirch was involved in heroin sales in any way. There were, for example, no records of bank deposits, net worth, or cash expenditures. *Id.* at 361-62. The deficiency was calculated based on an IRS agent's purely hypothetical calculation of what income would be realized from a given level of heroin sales each week over a given period of time. *Id.* at 359. Not only was the deficiency calculation completely divorced from any evidence of actual or inferrable heroin sales by Weimerskirch, but the entire method of calculation used was unsupported by evidence. *Id.*

The Commissioner's attempt to attach the presumption of correctness to the assessed deficiency in *Weimerskirch* was, in every sense of the word, naked.

In contrast, the presumption of correctness in the present case appears far more modestly appareled. The Commissioner's use of bank deposits as circumstantial evidence of gross income is an accepted methodology. *See, e.g., United States v. Ludwig*, 897 F.2d 875, 878 (7th Cir. 1990). The Tax Court found evidence that Kanter was engaged in income producing businesses. And the court found that actual deposits were made that had the appearance of income. *IRA*, 78 T.C.M. (CCH) at 1104; *see also United States v. Esser*, 520 F.2d 213, 217 (7th Cir. 1975) (describing test for implementing deposit analysis method of reconstructing income). There is no dispute about the evidence of deposits. Consequently, there was sufficient evidence to support the presumption of correctness.

Lastly, Kanter argues that the uncontradicted evidence at trial shows that the four deposits in question were loans and were not income. By uncontradicted, we can only assume Kanter means uncontradicted by any evidence beyond the evidence we have outlined, establishing, *prima facie*, that there was a deficiency during 1982. Because we have found that the Tax Court properly gave the Commissioner's assessed deficiency a presumption of correctness, we must interpret Kanter's argument as claiming that the evidence presented overcame the presumption. In that respect, Kanter's argument also fails.

In considering whether Kanter met his burden of proof, the Tax Court found Gallenberger's summary and Kanter's assertions unconvincing. "No credible evidence was introduced to support Kanter's assertion that the deposits were loans * * *. We find the testimony of the accountant, Gallenberger, unreliable and her analysis fatally flawed * * *." *IRA*, 78 T.C.M. (CCH) at 1104. The Tax Court also recalled

"Gallenberger's regular practice of record destruction" and the general lack of any documentation other than her summary and testimony. *Id.* at 1104-05. The evidence that Kanter asserts was "uncontradicted" was considered by the Tax Court and found wanting. Exhibit 9172PK, which, according to Kanter, demonstrates that the deposits from CPS, THC, and Administration Co. were loans, reflects a summary analysis by Linda Gallenberger that the Tax Court found not credible. Nor is it correct for Kanter to say that the Tax Court had determined previously that one of the deposits of money from Administration Co. was money already found to belong to Kanter. (Pet. Br. at 58.) Kanter cites to a sentence in the Tax Court's opinion as to issue 21 (allowable capital gains and losses in 1987) wherein the court states, "As indicated previously, funds from the Administration Co. special E and PSAC special E accounts were Kanter's funds." *IRA*, 78 T.C.M. (CCH) at 1126. This sentence, in context, refers only to the specific funds from the accounts cited and used in the specific transactions at issue (five years after the deposits at issue here) in that section of the Tax Court opinion. These specific funds were Kanter's own funds, and he was entitled, therefore, to the basis he had claimed for the assets he had purchased with those funds. But Kanter seeks to generalize this statement about his ownership of specific money to mean that all the money in the Special E accounts, at all times, already belonged to Kanter. The Tax Court's opinion does not say this.

In conclusion, the Tax Court did not clearly err in its findings regarding Kanter's unreported income in 1982 as determined by bank deposit analysis. These findings are therefore affirmed.

VI. Equitable Leasing's Payments to THC & Zion

A. Facts

Equitable Leasing Co., Inc. (Equitable) was the wholly owned company of Joel Mallin, a friend and former law partner of Kanter. Mallin used Equitable (among other companies) to promote and structure equipment leasing transactions to make money for investors. The investors' capital would be highly leveraged to purchase the equipment to be leased, and the residual value of the equipment at the end of the lease would provide the ostensible paper profit on the investors' capital. A principal motivation behind the investment in the leasing transactions, however, was the opportunity for tax benefits associated with the venture. Kanter acted as a middleman, introducing Mallin to investors for his leasing transactions. In return, Mallin paid commissions to Kanter entities. The Commissioner issued a notice of deficiency for 1983 that included a deficiency of $635,250 with respect to four payments by Equitable to Kanter entities, Zion, and THC.[26]

DATE	FORM OF PAYMENT	PAYEE	AMOUNT
Jan. 4, 1983[27]	Bank Transfer	Zion	$317,250
Jan. 24, 1983	Check	THC	$9500

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[26] THC was a Kanter-controlled investment company and Zion was a THC subsidiary. *See supra* note 24.

[27] The Tax Court opinion and the Commissioner's brief both indicate that this transfer occurred on January 8, 1983. It is of no significance to the disposition of the case, but the bank transfer record (Ex. 9203PK) and the THC adjusting journal entry (Ex. 146, entry 32) both indicate that the transfer took place on January 4, 1983.

June 1, 1983	Check	Zion	$6500
June 30, 1983	Bank Transfer	THC	$302,000
Total			$635,250

The Commissioner alleged that these payments were commissions paid for Kanter's procurement of investors in Mallin's enterprises. Kanter argued that Zion and THC were loaned money by Equitable that was then turned around and invested in Equitable as an accommodation to Equitable to enable it to close certain transactions.

The Tax Court found that there was sufficient evidence to indicate that Equitable had paid commissions to Zion and THC for Kanter's services in providing investors to Mallin. Two of the four payments, for $9500 and for $6500, were labeled (on the check in payment and in THC's adjusting journal entries, respectively) as commissions. The Tax Court determined that this evidence was sufficient to support the presumption that all of these payments to Zion and THC were income to Kanter. In response to this presumption, the Tax Court found that Kanter had provided no evidence other than his "uncorroborated, self-serving testimony" concerning the "accommodation" arrangement with Equitable. *IRA*, 78 T.C.M. (CCH) at 1103. The court found, as previously noted, that Kanter was not credible and that the four payments were income attributable to Kanter.

B. Analysis

Whether or not monies are taxable income to a taxpayer is a finding of fact that we review for clear error. *Reynolds*, 296 F.3d at 612. The Commissioner's assessment of a deficiency is presumed correct, but can be overcome by rebuttal evidence presented by the taxpayer. *Pittman*, 100 F.3d at 1313.

Kanter argues first that the Commissioner's assessment of a deficiency should not be given the benefit of the presumption of correctness because the Commissioner "failed to provide any evidence connecting Kanter to this income." (Pet. Br. at 59.) This argument fares no better here than it did when we considered it with respect to the Bank Deposit issue. There was evidence that Mallin and Kanter were partners in various investments, and that Kanter's law firm had procured investors for Mallin's Equitable Leasing transactions. (Tr. at 5213-15.) There was also evidence that Mallin had paid commissions for these services to Kanter entities. (*Id.*) Additionally, at least two of the payments in question were documented as commissions. This was sufficient evidence to provide a rational foundation for the Commissioner's assessment. The Commissioner's assessment appropriately received its presumption of correctness. *See Pittman*, 100 F.3d at 1313.

Kanter also argues that he has rebutted the Commissioner's deficiency with evidence that only the $16,000 that was labeled as commissions (comprised of the $9500 and $6500 checks) should be considered commission payments, and the remainder consisted of loans made as an accommodation to Equitable. Even accepting Kanter's concession that the $9500 and $6500 checks from Equitable Leasing to THC and Zion, respectively, were taxable commission income, we do not believe he has provided sufficient evidence to show that the two bank transfers of $317,350 and $302,000 were loans.

Regarding the $317,250 transfer, there is clearly evidence supporting the Tax Court's finding that the transfer was a commission paid to Zion, and Kanter has provided no evidence to rebut this finding despite his control of the entities involved and his access to the records of those entities. First, as noted, there was circumstantial evidence that Equitable Leasing was making payments to THC and Zion as commis-

sions. Additionally, THC's adjusting journal for 1983 has an entry "32" indicating an amount of $317,250 that was labeled, "Due from Zion – Commission Income to adj. for commiss. from Eq. Leasing, loaned to Zion on 1/4/83." (Ex. 146, THC adjusting journal at 6.) Finally, Kanter appears to concede in the facts section of his brief that this amount was received as commission. In his brief on appeal, Kanter breaks down the $635,250 as including "$317,250 as commission income from Equitable (see Ex. 146, THC adjusting journal, p. 6, adjusting journal entry 32, reflecting commission income of $317,250 which was paid to THC's subsidiary Zion as a loan from THC * * *)." (Pet. Br. at 16.) The Tax Court's finding that this payment was commission income was not clearly erroneous.

What about the June 30, 1983 transfer from Equitable to THC for $302,000? Against the general circumstantial evidence of commission payments to THC by Equitable and the presumption of correctness of the Commissioner's assessment of deficiency, there is an entry in THC's general ledger for June 30, 1983, for $302,000 labeled "Loan from Equitable Leasg." (Ex. 148, THC general ledger at 12.) Together with this entry there is an entry indicating an $8000 transfer three days earlier also labeled "Loan from Equitable Leasg." (*Id.*) This $8000 transfer is corroborated by a check from Equitable to THC on June 24, 1983, for $8000 that has a memo line reading, "loan." (Ex. 9203PK, check # 2391.) The corroboration of the general ledger entry for the $8000 transfer is indirectly probative of the likelihood that the roughly contemporaneous and similarly labeled ledger entry for the $302,000 transfer may also be correct. These circumstances make it more likely that the ledger is accurate in its indication that the $302,000 transfer was a loan and not a commission payment.

But there is one additional piece of evidence in the record that the Commissioner and Kanter have not mentioned. In

the THC adjusting journal, entry 59 is a barely legible entry for $310,000 that appears to read, "N/P – Equitable Leasing, Commission Income, to reclassify funds from Eq. Leasing." (Ex. 146, entry 59.) This entry is significant because we believe it may also represent the $302,000 and $8000 transfers and show that those transfers were commissions. These two transfers were roughly contemporaneous, and Kanter himself aggregates them and describes them as a cumulative amount in his brief. (*See* Pet. Br. at 16 ("$310,000 as loans from Equitable * * * reflecting a $302,000 loan and an $8,000 loan * * *.").) The $310,000 in entry 59 would appear to be the same as the $310,000 in the general ledger and as the $310,000 described by Kanter, comprising the total of the $8000 and $302,000 transfers. Entry 59 in the THC adjusting journal weighs against the general ledger's notations for both the $302,000 and the $8000 transfer and weighs further in favor of the Tax Court's finding that the $302,000 was a commission payment. In any event, this evidence does, at the very least, make the characterization of the $302,000 transfer unclear, and because Kanter bears the burden of rebutting the Commissioner's assessment of deficiency and controlled the entities whose records could have cleared this matter up definitively, we cannot say that the Tax Court clearly erred in finding that the $302,000 was a commission payment to THC for Kanter's services.

In conclusion, it was not clear error for the Tax Court to find that the transfers from Equitable Leasing were commissions and were taxable income.

VII. Cashmere Investment Assoc.'s transactions

A. Facts

During the 1970s, Kanter was involved in a series of real estate developments with developer Sam Zell. The development properties were owned by partnerships (real estate partnerships). Kanter's interests in the real estate partnerships

were held through a series of Kanter-controlled trusts, including the BWK Revocable Trust, the Everglades Trusts 1-5, and the BWK Family Trusts (referred to collectively as the grantor trusts). Each of these trusts was a grantor trust whose income was attributable to Kanter personally. A detailed breakdown of the real estate partnership interests and their associated financial attributes is provided in the Tax Court's opinion. *IRA*, 78 T.C.M. (CCH) at 1107-11. The interests in these real estate partnerships had, as of 1982-83, zero basis.

During 1982, Zell expressed his desire to purchase all of the real estate partnership interests held by the grantor trusts. Kanter was interested in selling to Zell, but was concerned that significant gains would be triggered by an unqualified sale of the real estate partnership interests held by his grantor trusts. The Tax Court found that twenty one of the real estate partnership interests held by the grantor trusts had negative capital accounts; that is, their liabilities exceeded their bases, by an amount, in total, of $476,889. *IRA*, 78 T.C.M. (CCH) at 1108. Therefore, the unqualified transfer of those interests would involve the assumption of liabilities in excess of the bases, and would trigger capital gains to the seller – Kanter, who was the owner by virtue of the IRC's grantor trust provisions. *See* 26 U.S.C. §§ 671-677.

In 1983, a series of transactions took place that ultimately resulted in the transfer of the real estate partnership interests from the grantor trusts to a Zell-controlled entity. The transfer took place in three stages.

1. Transfer of real estate partnership interests to Cashmere

Cashmere Investment Associates, Inc. (Cashmere) was an inactive "shelf" corporation incorporated in Delaware in 1982 and controlled by Kanter. On or about May 15, 1983, Kanter directed the grantor trusts to transfer their real estate partnership interests to Cashmere in what was intended as a

nontaxable exchange under 26 U.S.C. § 351 in return for Cashmere common and preferred stock. Concurrently with the § 351 transfer, the grantor trusts also transferred to Cashmere eight promissory notes payable to, and held by, the grantor trusts with a face value, in total, of $498,500. The promissory notes were all dated May 1, 1983, and were payable on August 1, 1983. These promissory notes, according to Kanter, had a basis equal to face value and increased the total aggregate basis of the transferred property so as to eliminate the gain that would otherwise have been realized under 26 U.S.C. § 357(c) through the assumption by Cashmere of the negative capital accounts in the transfer of the real estate partnership interests. *See* 26 U.S.C. § 357(c).[28]

2. Sale of Cashmere stock to Waco

On July 12, 1983, in the next stage of the transfers to Zell-controlled entities, Kanter directed the grantor trusts to sell their common and preferred stock in Cashmere to Waco Capital Corp. in return for promissory installment notes totaling approximately $1.5 million. The grantor trusts reported the income from this sale under the installment method of 26 U.S.C. § 453.

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[28] Section 357(c) provides in relevant part:

> (c) Liabilities in excess of basis.–
>
> (1) In general. In the case of an exchange –
>
> (A) to which section 351 applies * * *
>
> if the sum of the amount of the liabilities assumed exceeds the total of the adjusted basis of the property transferred pursuant to such exchange, then such excess shall be considered as a gain from the sale or exchange of a capital asset or of property which is not a capital asset, as the case may be.

26 U.S.C. § 357(c).

Waco was a Delaware corporation whose sole shareholder was BRT. BRT's beneficiaries were the members of Kanter's family, who were also the beneficiaries of the grantor trusts. The Tax Court found that, under 26 U.S.C. § 453(f), Waco and the grantor trusts were "related persons." *See* 26 U.S.C. § 318(a)(2), (3).

On August 31, 1983, the promissory notes held by Cashmere were paid off by eight checks drawn on the Administration Co.'s Special E account. As noted, the Special E account contained the commingled funds of a variety of entities, mostly (if not entirely) Kanter entities, and the Administration Co. accounted internally for the specific source of a given disbursement. The Administration Co.'s general ledger, however, did not specify the source of the eight checks paying the notes. The checks themselves indicate, in part, what entity is the payor of the notes. Three of the promissory notes were ostensibly paid with funds from BRT, an entity that was not the maker of the notes in question, and there was no documentary evidence that BRT was advancing the funds to the makers of the promissory notes or had, in some way, assumed the obligations on the notes. *IRA*, 78 T.C.M. (CCH) at 1110-11.

As of September 1, Waco held all of the stock in Cashmere, and Cashmere's assets included the real estate partnership interests and $498,500 in cash (from the note payments).

3. Sale of Cashmere stock from Waco to Zell

Kanter subsequently negotiated the sale of Waco's Cashmere stock to Equity Financial Management Co. (Equity), an entity controlled by Zell. On September 2, 1983, Waco sold the Cashmere stock to Equity for $1,647,500 pay-

able by check.[29] Immediately after the purchase, Zell liquidated Cashmere.

The Tax Court found that this convoluted series of transactions taking place within a three-and-one-half month period that ultimately resulted in the transfer of the real estate partnership interests to Zell was arranged principally to avoid immediate recognition of gain on the transfer and otherwise lacked any bona fide business purpose. *IRA*, 78 T.C.M. (CCH) at 1113; see 26 U.S.C. § 357(b)(1)(A), (B). Therefore, the assumption of liabilities by Cashmere was recognized as money received by Kanter (through his grantor trusts), and he was required to be taxed on his gain resulting from the transfer, up to the full amount of the liabilities. 26 U.S.C. § 357(b). Additionally, the Tax Court found that the transfer of the notes with the real estate partnership interests also lacked any bona fide business purpose and were principally intended as a means to avoid income tax. The Tax Court found that the notes represented mere transfers between and among Kanter-controlled entities, and did not represent true indebtedness. Therefore, Kanter had no basis in the notes, and the notes did not, therefore, increase the aggregate basis in the property transferred to Cashmere. Under § 357(c), the excess of liabilities over basis in the transferred property was therefore recognized as capital gain to Kanter. Because the basis in the partnership interests was zero, under both § 357(b) and (c), the full amount of the transferred liabilities was taxable to Kanter.

Additionally, the Tax Court found that the subsequent sale to Waco using the installment method was a "dis-

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[29] As noted, Cashmere's assets included $498,500 in cash plus the partnership interests. Therefore, the $1,647,500 purchase price of Cashmere included a purchase price of $1,149,000 for the real estate partnership interests.

pos[ition] of property to a related person." 26 U.S.C. § 453(e)(1)(A). When Waco then subsequently transferred, within two years, the Cashmere stock to Equity, the installment method of reporting was no longer available. 26 U.S.C. § 453(e)(1), (2). The entire amount realized by Waco in the second disposition was treated as received (at the time of the second disposition) by the seller-grantor trusts in the first disposition. *Id.*

B. Analysis

Whether the transactions involving Cashmere had economic substance for federal income tax purposes is a factual question reviewed for clear error. *N. Ind. Pub. Serv. Co. v. Comm'r*, 115 F.3d 506, 510 (7th Cir. 1997). Similarly, whether the installment method of reporting is available is a factual question that we review for clear error. *Applegate v. Comm'r*, 980 F.2d 1125, 1128 (7th Cir. 1992).

1. The Attempted § 351 Transaction

The tax-free transfer of property to a controlled corporation solely in exchange for the transferee corporation's stock is permitted under 26 U.S.C. § 351. The IRC also provides a means for preserving § 351 eligibility in circumstances where the transferee corporation assumes liabilities of the transferor together with the property transferred (an event that is economically equivalent to a transfer of money (boot) from the transferee corporation to the property transferor). 26 U.S.C. § 357. There are two limitations, however, to tax-free treatment under § 351. First, the taxpayer-transferor must prove by a preponderance of the evidence that the liabilities were not transferred for the principal purpose of tax avoidance and that the transfer had a bona fide business purpose. § 357(b). If the taxpayer fails to clear this hurdle, the assumption of the liability is treated as money received by the taxpayer, and the taxpayer recognizes any gain to the full amount of the liability. 26 U.S.C. §§ 357(b)(1), 351(b)(1)(A). Second, if the

amount of the liability transferred is greater than the basis of the property transferred, then, in general, the transferor-taxpayer recognizes a capital gain on the amount by which the liability exceeds the basis of the transferred property. 26 U.S.C. § 357(c)(1).

a. 26 U.S.C. § 357(b)

There can be little question that the Tax Court was correct when it viewed the totality of the convoluted Cashmere transactions and found that their only purpose was the avoidance of federal income tax. Kanter's argument that § 357(b)(1) does not reach this transaction is meritless. Within a four-month period of time an inactive shelf corporation controlled by Kanter (Cashmere) had its stock transferred three times, twice between Kanter-controlled entities. Within that same time span, promissory notes, virtually equal in total value to the total negative capital account balances, were made by entities controlled by Kanter, transferred (along with the real estate partnership interests holding the negative balances) to entities controlled by Kanter and then satisfied by entities controlled by Kanter. Both Cashmere and the promissory notes completed their entire useful life-cycle within the span of the larger, intended transaction – transferring the real estate partnership interests to Zell. Yet neither the promissory notes nor Cashmere functioned to facilitate the transfer of the real estate partnership interests to Zell: the promissory notes were created, transferred, and satisfied before the consummation of the sale to Zell, and Cashmere was liquidated as soon as its stock came into Zell's possession leaving Zell with only the desired asset – the real estate partnership interests. The entire transaction was constructed to avoid the recognition of the gain realized on the assumption of the real estate partnerships' liabilities (by, ultimately, Zell). Therefore, the assumption of those liabilities by Cashmere in the initial stages of the process cannot be de-

scribed as other than having as its principal purpose the avoidance of federal income tax. *See* 26 U.S.C. § 357(b).

Kanter's remaining argument with respect to § 357(b) appears to be that the intent of that statutory section was to prevent taxpayers from creating additional liabilities (like personal loans or debts) to be packaged with assets contributed in a § 351 exchange in order to extract the gains contained within the contributed property without recognition for tax purposes. This kind of intent to avoid taxes, argues Kanter, is far removed from the present case where the liabilities were a substantial aspect of the real estate partnership interests to be contributed. This argument fails as well. The fact that the liabilities being contributed were "ordinary business liabilities of the partnerships" does nothing to save this transaction. As noted, the entire business of contributing the partnership interests and their associated liabilities to Cashmere was a transaction whose only function was the avoidance of federal tax. Therefore, "taking into consideration the nature of the liability and the circumstances in the light of which the arrangement for the assumption was made," it is clear that the principal purpose of the assumption of liabilities was the avoidance of tax. 26 U.S.C. § 357(b)(1).

It was not clearly erroneous for the Tax Court to have found that the assumption of the real estate partnership interests' liabilities by Cashmere had as its principal purpose the avoidance of federal income tax.

b. 26 U.S.C. § 357(c)

The Tax Court also found, alternatively, that § 357(c) would apply to the Cashmere transactions.[30] Section

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[30] Section 357(c)(2)(A) gives priority to § 357(b)(1) when both § 357(c) and § 357(b)(1) apply. Therefore, the finding under

§ 357(c) is triggered when the amount of the liabilities assumed exceeds the basis of the property contributed in the § 351 exchange. The taxpayer is taxed on the amount by which the liabilities exceed the basis. The Tax Court found that the contributed promissory notes did not represent genuine indebtedness and had, therefore, a basis of zero. Without any additional basis from the promissory notes, the basis of the contributed real estate partnership interests was zero, and the amount of the liabilities assumed (in the form of the oft-mentioned negative capital accounts) necessarily exceeded that zero basis. Therefore, the gain realized in the § 351 transfer must be recognized to the full extent of the assumed liabilities.

Kanter vigorously argues that the substance of the promissory notes should be respected and not disregarded as mere form, and the notes should be given a basis equal to their face value. For this argument Kanter relies heavily on the Ninth Circuit's determinations in *Peracchi v. Comm'r*, 143 F.3d 487 (9th Cir. 1998), where a taxpayer made and contributed notes to his closely held corporation. The Ninth Circuit found substance in Peracchi's promises to pay himself, and increased the basis of property contributed (in a § 351 exchange) to a figure greater than the liabilities assumed by the closely-held transferee corporation. *Id.; see also Lessinger v. Comm'r*, 872 F.2d 519 (2d Cir. 1989) (finding also that personal note had face-value basis in hands of transferee corporation). The hypothetical risk that this note might somehow become the property of a creditor (through bankruptcy of the corporation) and that a creditor might then be able to enforce the note was sufficient to make the note more than an empty promise. *Peracchi*, 143 F.3d at 493. The Ninth Circuit panel

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§ 357(c) is only relevant as the alternative to the previous finding under § 357(b)(1).

realized the potential for abuse of this holding, however, and cabined it.

> We confine our holding to a case such as this where the note is contributed to an operating business which is subject to a non-trivial risk of bankruptcy or receivership. [The closely held company] is not, for example, a shell corporation or a passive investment company.

Id. at 493 n.14.

Even if we were to accept *Peracchi*'s underlying premise that a taxpayer's self-made obligations to his own closely held corporation should be respected for tax purposes, in light of the language limiting *Peracchi*'s holding, we would not extend that premise to the present case. Cashmere was a passive investment company that, before the transactions at issue, was a shelf corporation. And after the transfer of the real estate partnership interests to Zell, Cashmere was liquidated. Cashmere was not an operating business, and, unlike *Peracchi*, where an insurance corporation needed more assets to meet a minimum premium-to-asset ratio for regulatory purposes, there was no underlying business purpose here for these transitory promissory notes. Nor did Cashmere face a "non-trivial risk of bankruptcy." *Peracchi* is, therefore, quite distinguishable from the present case. The promissory notes here did not represent genuine indebtedness, and the Tax Court did not clearly err in finding that the promissory notes had no basis. Therefore, the Tax Court's conclusion that the liabilities assumed exceeded the basis of the contributed property by the full amount of the liabilities and were taxable to that extent was not clearly erroneous.

2. Disallowance of § 453 Installment Method

The next steps in the sale of the real estate partnership interests to Zell involved, first, the sale of the Cashmere stock from Kanter's grantor trusts to Waco and, second, the subsequent sale within two months of the Cashmere stock from

Waco to Equity (the Zell-controlled entity). The grantor trusts reported their gains from the sale to Waco under the installment method allowed by 26 U.S.C. § 453.[31] But § 453(e) limits the use of the installment method in circumstances where there is a second disposition of the property within two years that is effected by a person "related" to the original seller. In other words, if A sells to B, and then B sells to C (within two years), A cannot report the income from its sale under the installment method if A and B are "related persons" under 26 U.S.C. §§ 267(b) or 318(a). The Tax Court found that the grantor trusts and Waco were "related persons," and that the entire amount of income attributable to the sale of the Cashmere stock to Waco must be recognized in 1983. We affirm this finding as well.

Section § 453(f)(1) defines a "related person" for purposes of determining the reach of § 453(e):

> (A) a person whose stock would be attributed under section 318(a) (other than paragraph (4) thereof) to the person first disposing of the property, or
>
> (B) a person who bears a relationship described in section 267(b) to the person first disposing of the property.

26 U.S.C. § 453(f)(1). Waco's stock is owned entirely by BRT, whose beneficiaries were undisputedly the members of Kanter's family. Similarly, Kanter does not dispute that these

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[31] Section § 453(c) states:

> For purposes of this section, the term "installment method" means a method of payment under which the income recognized for any taxable year from a disposition is that proportion of the payments received in that year which the gross profit (realized or to be realized when payment is completed) bears to the total contract price.

26 U.S.C. § 453(c).

same family members were the beneficiaries of the grantor trusts. Under 26 U.S.C. § 318(a)(2)(B)(i), the stock owned by BRT is considered owned by its beneficiaries. Therefore, the BRT beneficiaries are treated as owning the Waco stock. Similarly, those same BRT beneficiaries are also beneficiaries of the grantor trusts, and their ownership of the Waco stock is imputed "upstream," under § 318(a)(3)(B)(i), to the grantor trusts. Therefore, the stock of Waco would be attributed to the grantor trusts under § 318(a), making Waco a person "related" to the grantor trusts under § 453(f)(1)(A). The attribution, therefore, makes the sale of the Cashmere stock to Waco ineligible for the installment method under § 453(e).[32]

Similarly, as noted in Part III, Kanter was the substantial owner of BRT under the grantor trust provisions of 26 U.S.C. §§ 671 *et seq.* Therefore, there is an alternative means by which the grantor trusts and Waco are "related persons."[33]

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[32] We note with some trepidation that there was no effort by the Tax Court to identify the precise actuarial interests of the beneficiaries of BRT nor how precisely those beneficiaries' identities matched the beneficiaries of the grantor trusts. This information would be relevant for determining the exact percentage of Waco stock owned by the BRT beneficiaries (who were also grantor trust beneficiaries), which would then be imputed to the grantor trusts. Because Kanter did not make this argument on this issue, however, we will not disturb the Tax Court's determination. *United States v. Jones*, 34 F.3d 495, 499 (7th Cir. 1994) (finding argument not made before this court in opening brief is waived).

[33] There does not appear to be any obstacle in the statute, legislative history, or regulations to the attribution of a grantor trust's stock ownership to the beneficiaries of a trust as well as to the substantial owner of a trust under §§ 671 *et seq.* *See The Attribution Rules*, 554-2d Tax Mgmt. Portfolio at A-11 (1996) ("Apparently, attribution from the [grantor] trust to the beneficiaries and from the beneficiaries to the trust would still occur, even if the grantor or

Under § 318(a)(2)(B)(ii), stock owned by a grantor trust is attributed to its grantor; BRT's stock, therefore, is attributed to Kanter. That is, Kanter himself is considered to own the Waco stock owned by BRT. Following a similar statutory path as before, Kanter's status as the substantial owner of the grantor trusts means that any stock he owns personally is attributed to the grantor trusts under § 318(a)(3)(B)(ii). Therefore, Kanter's attributed ownership of the Waco stock means that the grantor trusts also own the Waco stock. Because the grantor trusts are attributed ownership of the Waco stock under § 318(a), Waco and the grantor trusts are "related persons" under § 453(f)(1)(A), and the sale of the Cashmere stock from the grantor trusts to Waco is ineligible for reporting under the installment method by operation of § 453(e).

Whether one, the other, or both methods of analysis are followed, the grantor trusts' sale of Cashmere stock to Waco was ineligible for the installment method of reporting for federal income tax purposes. The Tax Court's findings on this issue were not clearly erroneous.

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another is deemed to be the 'owner,' although the statute and legislative history are ambiguous on this point and the regulations are silent."). Nor does any court appear to have ruled on the issue. Our research unearthed only one commentator who has suggested that attribution to a grantor precludes attribution to the beneficiaries. *See* Shop Talk, *Is Stock Attributed to Beneficiaries of Grantor Trusts?*, 65 J. TAX'N 207 (Burton W. Kanter & Sheldon I. Banoff ed., 1986) ("A common sense interpretation of Section 318(a)(2)(B)(ii) should be that its specific rule regarding attribution from grantor trusts should preempt the general rule of trust attribution of Section 318(a)(2)(B)(i)."). The financial interest in this matter of one of the editors of the article may diminish the persuasive value of the proposed answer.

VIII. Naomi Kanter motions

A. Facts

On May 8, 2001, in the midst of the Tax Court's post-trial Rule 155 computations, attorney Karen Hawkins entered an appearance in the Tax Court on behalf of Kanter's wife, Naomi Kanter (Naomi), for the purpose of claiming that Naomi should not be jointly and severally liable for the Tax Court's determined deficiencies against Kanter. Shortly thereafter, Randall Dick, attorney of record for both Kanter and Naomi, moved to withdraw his representation of Naomi. By her new counsel, Naomi first filed a series of objections to the Commissioner's computations because they held Naomi liable for fraud penalties. The Tax Court upheld these objections. (Order, *IRA*, 6/20/01; App. at 0346.) Naomi then filed seven motions asking the Tax Court to find that she had not meaningfully participated in the litigation as provided in 26 U.S.C. § 6015(g)(2). In the alternative, Naomi asked that the Tax Court reopen the record in order to hear additional evidence that Naomi was an "innocent spouse" under 26 U.S.C. § 6015(b) and § 6015(f), and not jointly and severally liable with her husband. In response to Naomi's motion, the Commissioner stated that "respondent has no objection to petitioner's first request for relief [a finding that Naomi had not meaningfully participated in the litigation]." (*See* App. at 0364.) Therefore, the Commissioner felt the alternative request to reopen to hear additional evidence that Naomi was an innocent spouse was moot.

In its September 20, 2001 Order, the Tax Court denied Naomi's seven motions. (*See* App. at 0224.) The Tax Court found that the language of § 6015(g)(2) required that any finding that a spouse had not "meaningfully participated" in the litigation must occur in a subsequent, separate proceeding that could properly consider the matter now before us as a "prior proceeding." 26 U.S.C. § 6015(g)(2). Therefore, the Tax Court ruled, Naomi would have to wait for a separate

proceeding before the Tax Court to have the res judicata effect of the present case adjudicated. Additionally, the Tax Court exercised its discretion not to reopen the record and take additional evidence on the merits of Naomi's claim that she was an "innocent spouse." The Tax Court found that, even though the innocent-spouse provisions had been significantly amended in 1998, and clarified in 2000, the underlying availability of innocent-spouse relief had been unchanged since the origination of the present case in the early 1990s. The court refused to reopen a case whose trial had concluded more than five years earlier, especially when there had been no mention of innocent-spouse relief during the period since the trial. Given the possibility of later relief for Naomi in a subsequent proceeding, the Tax Court did not feel the burden on the Commissioner to reopen the present case and litigate the issue was justified.

B. Analysis

This court reviews the denial of motions to reopen the Tax Court's record for abuse of discretion. *Coleman v. Comm'r*, 16 F.3d 821, 829 (7th Cir. 1994). Whether or not § 6015(g)(2) requires a subsequent proceeding to determine whether Naomi had "meaningfully participated" in the matter now before us as a "prior proceeding" is a question of statutory interpretation that we review *de novo*. *Eli Lilly & Co. v. Natural Answers, Inc.*, 233 F.3d 456, 467 (7th Cir. 2000).

The substance of current 26 U.S.C. § 6015 was enacted as part of the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat 685, § 3201 (IRRRA). Technical corrections to the IRRRA were enacted in 2000, leaving us with the statute as it presently appears. *See* Community Renewal Tax Relief Act of 2000, Pub. L. No. 106-554, 114 Stat. 2763, App. G. Section 6015 contains the so-called "innocent spouse" provisions that allow a spouse to avoid joint and several liability for a tax deficiency assessed against both husband and wife based on a joint tax

return filing. To avoid joint and several liability, the innocent spouse must show, generally, that (1) a joint return was filed, (2) the return understated the tax owed based on the "erroneous items" of the other joint filer, (3) she did not know, and had no reason to know, that there was an understatement, (4) it is inequitable to hold her liable for the understatement and (5) she has applied for innocent-spouse protection no later than two years after the Commissioner begins "collection activities." *See* 26 U.S.C. § 6015(b). Section 6015 expanded previous innocent-spouse provisions by removing the requirement that the understatement be "substantial" and that the return be "grossly erroneous" in order to receive protection. Additionally, § 6015 provided increased protection for divorced or separated spouses by holding such a spouse liable for only those items on which she would have been liable had she filed a separate return. Finally, the modifications to § 6015 provided for equitable relief for an innocent spouse. 26 U.S.C. § 6015; *see also* John B. Harper, *Federal Tax Relief for Innocent Spouses: New Opportunities Under the IRS Restructuring and Reform Act of 1998*, 61 ALA. LAW. 204 (2000).

Section 6015 also contemplates the possibility that a court will adjudicate a joint tax liability to completion before an innocent spouse invokes the section's protection. Under § 6015, res judicata will attach to the decision of a court if the innocent spouse "participated meaningfully in [the] prior proceeding," even if the innocent-spouse issue was never presented to the adjudicating court. 26 U.S.C. § 6015(g)(2).

Naomi first argues that the Tax Court should have "determined," under § 6015(g)(2), that she did not meaningfully participate in the Tax Court litigation and that the Tax Court's *IRA* decision against her husband would have had no preclusive effect with respect to her potential innocent-spouse defense to joint liability. Naomi argues that the record and the Tax Court's decision clearly show that she was

not involved in the present case. *See IRA*, 78 T.C.M.(CCH) at 969 ("Petitioner Naomi R. Kanter, Kanter's wife, was not involved in any of the activities giving rise to this litigation. However, she filed joint Federal income tax returns with Kanter for the years at issue."). She further notes that there would likely not be any delay in the course of the present case with such a determination, that there would be no need to reopen the record in order to make such a determination, and that the Commissioner expressly noticed no objection to such a determination.

Unfortunately for Naomi, the general principles of res judicata and the language of the statute deny her this relief at this time. Section 6015(g)(2) is only properly invoked in a subsequent judicial proceeding to avoid the preclusive effect of a prior judicial determination, and has no application during the pendency of the initial judicial proceeding whose preclusive effect she wishes to avoid. First, we start with the plain language of the statute. *Lara-Ruiz v. INS*, 241 F.3d 934, 940 (7th Cir. 2001). As the Tax Court observed, the plain language of § 6015(g)(2), which is labeled "Res judicata," limits its effect to consideration of a "decision of a court in any prior proceeding," to determine if an "individual participated meaningfully in such prior proceeding." To us, this language is clear: a decision from a prior proceeding means that this statute is only applicable when the original court proceeding determining tax liability has concluded. We can only conclude that this section is designed to assist innocent spouses in avoiding the preclusive effect of the other spouse's prior, completely adjudicated court case, but that the section has no application internal to the prior judicial proceeding.

This reading gains support from the general principle of res judicata. Res judicata prevents parties from relitigating claims that have already been adjudicated by a court to a final judgment on the merits. Of necessity, res judicata re-

quires two proceedings: an original proceeding wherein a final judgment on the merits is rendered, and a subsequent proceeding wherein a party seeks to litigate again a claim decided in the original proceeding. *See N.H. v. Me.*, 532 U.S. 742, 748 (2001) ("Claim preclusion [res judicata] generally refers to the effect of a *prior* judgment in foreclosing *successive* litigation of the very same claim, whether or not relitigation of the claim raises the same issues as the *earlier* suit.") (emphasis added); *see also* BLACK'S LAW DICTIONARY 1305 (6th ed. 1990) (defining res judicata as the "[r]ule that a final judgment rendered by a court * * * constitutes an absolute bar to a *subsequent* action involving the same claim.") (emphasis added). Therefore, Naomi cannot have the level of her meaningful participation (or lack thereof) in the present case determined until res judicata becomes relevant in a subsequent proceeding.

In the alternative, Naomi argues that, if she must wait for a subsequent proceeding before § 6015(g)(2) becomes relevant, she wants to have her innocent-spouse defense to joint liability (under 26 U.S.C. § 6015(b) & (f)) adjudicated on the merits during the pendency of the present case. This would require, she argues, reopening the record and allowing her to introduce the necessary evidence to support her innocent-spouse claim, and she further claims that it was an abuse of discretion for the Tax Court not to allow her to do so.

Naomi seeks support in prior Tax Court decisions that, he claims, have "bifurcated proceedings" in order to allow an innocent spouse to have issues of joint liability tried proximately to the general issues of tax liability. (Pet. Br. at 78.) Yet in none of the cases upon which Naomi relies did the innocent spouse remain silent for the duration of the Tax Court proceedings (with over ten years elapsing from Kanter's petition to Naomi's first motion regarding this issue) and, only after the case was all but closed, raise, for the first time, an innocent-spouse defense to joint liability. In

Vetrano v. Comm'r, 116 T.C. 272 (2001), the innocent-spouse defense was asserted in the original petition to the Tax Court. *Id.* at 274. Likewise, both spouses in *Charlton v. Comm'r*, 114 T.C. 333 (2000), asserted in their original petitions that they qualified for innocent-spouse relief. *Id.* at 338. In *King v. Comm'r*, 116 T.C. 198 (2001), the original petition was, in its entirety, an innocent-spouse defense, and the so-called not-innocent spouse was involved as an intervenor. The one consistent thread running through all of these cases relied upon by Naomi is that the request for innocent-spouse relief was squarely before the Tax Court well before the resolution of the case. Naomi, for whatever reason, never put the Tax Court on notice that she had an innocent-spouse defense to joint liability.

Naomi claims her silence was due, in part, to a conflict of interest with respect to the joint representation by counsel of her and her husband. This conflict of interest, she alleges, is the kind of extraordinary circumstance that makes refusing to reopen the record an abuse of discretion. What Naomi fails to argue adequately, however, is that there was an actual conflict of interest. Joint representation, by itself, is not a conflict of interest; the representation of one client must actually conflict with the representation of the other. *See United States v. Fox*, 613 F.2d 99, 102 (5th Cir. 1980) ("However, an actual, not merely hypothetical or speculative, conflict must be demonstrated before it can be said that an accused has been deprived of effective assistance of counsel."); *cf. Dorchester Indus., Inc. v. Comm'r*, 108 T.C. 320, 339 (1997) ("Certainly, one spouse's claim that she (he) is an innocent spouse can present a conflict of interest to counsel trying to represent both spouses. If, indeed, the spouses do have differing interests with respect to any issue in a case, our rules provide that counsel must secure informed consent of the client, withdraw from the case, or take whatever other steps are necessary to obviate the conflict of interest."). Naomi shows

no actual conflict in the joint representation of her and her husband during the present case. If Naomi could point us to an innocent-spouse defense that she had at any time during the trial, before a decision by the Tax Court, that would have relied upon arguments in conflict with Kanter's defenses, then she is correct that Tax Court Rule 24(g) may have required separate representation. *See Dorchester Indus.*, 108 T.C. at 339. She has not yet alleged such an argument – in other words, she does not show us that she ever had a viable innocent-spouse defense that she was prevented from raising because it conflicted with Kanter's defense strategy. There does not appear to have ever been a time when she could say that the joint representation faced conflicting interests between Naomi and Kanter. Now, with the Tax Court's having entered a final decision, Naomi would have us engage in hindsight and find that she was inevitably prejudiced by the joint representation because she is now liable for deficiencies for which she is the "innocent spouse." Had Kanter's arguments succeeded in the Tax Court, she would not be facing joint liability nor would she be alleging conflict of interest. We cannot, and will not, automatically conclude that her silence was helpless ignorance and not a strategic decision.

Naomi is not prejudiced by the Tax Court's refusal to reopen the record. The opportunity to assert innocent-spouse defenses to joint and several liability remains fully available to her for up to two years after the Commissioner's first "collection activity." 26 U.S.C. § 6015(b)(1)(E).[34] She will have

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[34] Collection activity is defined in Treasury Regulation 1.6015-5(b)(2)(i) as

> [A] section 6330 notice; an offset of an overpayment of the [innocent] spouse against a liability under section 6402; the filing of a suit by the United States against the [innocent] spouse for the collection of the joint tax liability; or the filing of a claim by the United States in a court proceeding in which the

her asserted defense administratively reviewed by the IRS, and, if necessary and appropriate, judicially reviewed by the Tax Court.[35]

The Tax Court's decision not to determine that Naomi had not "participated meaningfully" in the present litigation was proper under § 6015(g)(2), and it was not an abuse of discretion for the court to refuse to reopen the record in order to receive evidence concerning an innocent-spouse defense.

CONCLUSION

In summary:

Issue I – STJ Report. Because we take the Tax Court at its word that in rendering its final opinion it agreed with and adopted the opinion of Special Trial Judge Couvillion, we find Kanter's arguments challenging the Tax Court's refusal

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> [innocent] spouse is a party or which involves property of the [innocent] spouse. Collection activity does not include a notice of deficiency; the filing of a Notice of Federal Tax Lien; or a demand for payment of tax.

26 C.F.R. § 1.6015-5(b)(2)(i).

[35] We do not, obviously, determine on the merits as part of this appeal whether Naomi "meaningfully participated" in the litigation in the present case so that res judicata would (or would not) apply. We, however, note again the Tax Court's finding that Naomi was not involved in the activities underlying the present case, *IRA*, 78 T.C.M. (CCH) at 969 ("Petitioner Naomi R. Kanter, Kanter's wife, was not involved in any of the activities giving rise to this litigation."), and the Commissioner's response in the record that he did not object to a finding that Naomi had not meaningfully participated within the meaning of § 6015(g)(2), (App. at 0364 ("For the purposes of this case, respondent has no objection to petitioner's first request for relief [finding that she had not meaningfully participated in the litigation].")), as indicia relevant to such a determination.

to disclose the STJ's "original" report moot. We AFFIRM the Tax Court's denial of Kanter's motions for access to the STJ's report.

Issue II – Fraud. There is significant circumstantial evidence of fraudulent intent. It was not clearly erroneous for the Tax Court to find fraud. We AFFIRM the Tax Court's findings on this issue.

Issue III – BRT. It was not clearly erroneous for the Tax Court to find that Kanter was the grantor of BRT and to affirm deficiencies against him for BRT's income during the years at issue. We AFFIRM the Tax Court's findings on this issue.

Issue IV – Washington Painting. There can be no question that Kanter sought to facilitate the sale of the George Washington painting for profit. The Tax Court found that, in every instance where the potential for profit was involved, Kanter engaged in significant non-law-related business activities with the purpose of facilitating the business opportunities of others for his own profit. Given the number of evidentiary indicators supporting that this venture was also for profit, we believe it was clearly erroneous to find otherwise. We REVERSE the Tax Court's findings on this issue.

Issue V – Bank Deposits. The Tax Court did not clearly err in its findings regarding Kanter's unreported income in 1982 as determined by bank deposit analysis. We AFFIRM the Tax Court's findings on this issue.

Issue VI – Equitable. It was not clear error for the Tax Court to find that the transfers from Equitable Leasing were commissions and were taxable income. We AFFIRM the Tax Court's findings on this issue.

Issue VII – Cashmere. It was not clearly erroneous for the Tax Court to have found that the assumption of the real estate partnership interests' liabilities by Cashmere had as its

principal purpose the avoidance of federal income tax. Alternatively, it was not clearly erroneous for the Tax Court to conclude that the promissory notes did not represent genuine indebtedness and had no basis, and, therefore, that the liabilities assumed exceeded the basis of the contributed property by the full amount of the liabilities and were taxable to that extent. Finally, the Tax Court did not clearly err in finding the grantor trusts' sale of Cashmere stock to Waco ineligible for the installment method of reporting for federal income tax purposes. We AFFIRM the Tax Court's findings on this issue.

Issue VIII – Naomi Kanter. We believe the Tax Court's interpretation of § 6015(g) was correct, and that Naomi must wait for a subsequent proceeding before she can have the level of her participation in the present case determined. We also do not believe that it was an abuse of discretion for the Tax Court to refuse to reopen the present case to allow Naomi to litigate her innocent-spouse defense. We AFFIRM the Tax Court on this issue.

For the foregoing reasons we AFFIRM in part and REVERSE in part the decision of the Tax Court.

CUDAHY, Circuit Judge, concurring in part, dissenting in part.

I concur with the majority's opinion as to Naomi Kanter's issues on appeal, but dissent otherwise. I write separately to address Kanter's threshold argument that the Special Trial Judge's ("STJ's") original report must be made a part of the record on appeal so that this court can determine whether its contents have been adequately considered by the Tax Court judge, whose opinion is before us.

Before I begin the legal analysis that, I believe, demonstrates why the withholding of the report is improper, I want

to take a few lines to address the policy concerns that leap to mind when first encountering the suppression of the report. For the Tax Court is "not" merely "unusual;" it is, I believe, unique among all the institutions in the law where one official conducts a trial (and thus hears the witnesses) and prepares a report or other document containing her findings or recommendations based on the trial, and another official or group of officials subsequently makes the operative decision. Even the Commissioner, at oral argument, acknowledged that in every milieu except that of the Tax Court, the document containing the findings or recommendations of the official conducting the trial are available to a court reviewing the operative decision. This includes, for example, the report of a federal magistrate judge to a district court responsible for a decision. This is also the practice under the Administrative Procedure Act which governs practically all federal administrative proceedings and where the hearing officer (usually an administrative law judge) must file a recommended decision which is distributed to both parties, any appellate court conducting a review and to the public at large. Transparency is the universal practice of agencies and courts employing these decisional practices. The question then becomes, if there are policy reasons that dictate transparency for everyone else, why do these reasons not apply to the Tax Court?

The Tax Court has not denied that a document containing the original findings of the STJ exists, yet it refuses to include this document in the record on appeal. It is no answer at all to claim that the report of the STJ is like a law clerk's memorandum to a judge or the memorandum of a fellow jurist on a panel – an internal privileged decisional document. The document here is of an official who presided over the trial and heard the witnesses, and it is directed towards an official who has no first hand knowledge of any aspect of that same trial. I am not impugning the integrity of the Tax Court judges here, or at any point in this dissent; I am merely

questioning the propriety of their denial of procedural transparency in a circumstance where every other like process known to the law is transparent. If we approve the Tax Court's practice here, are we not suggesting to the whole administrative array of the federal government that it may seek by available means when statutes permit to deny transparency when engaging in like decisional processes? I believe that the legal analysis of the majority as well as my own must be examined in the context of the larger implications of allowing an administrative body (technically, an Article I court) like the Tax Court to flout the otherwise ubiquitous principle of transparency in its proceedings. That said, I believe there also exist sound constitutional grounds demanding transparency in this instance.

As a threshold matter, everyone agrees that Kanter's arguments are immaterial if the Tax Court's opinion is the verbatim reproduction of the STJ's report, which the majority and the Eleventh Circuit, *Ballard v. Commissioner*, 321 F.3d 1037 (11th Cir. 2003), appear to believe is the case, and which the Tax Court's opinion superficially purports to be. The Tax Court's opinion clearly states that it adopts and agrees with the "opinion" of the STJ. If that recital is to be interpreted as meaning that the STJ's initial report lies before us already, then there is no issue of the Tax Court judge's according due regard or a presumption of correctness to the STJ's findings. Deference would not be an issue if there has been outright adoption of the STJ's findings. This state of affairs would also appear to moot Kanter's due process argument as well as his Rule 183 argument. Kanter relies on *United States v. Raddatz*, 447 U.S. 667, to argue that an STJ should be treated the same as a magistrate judge. Using *Raddatz*, Kanter argues that when the Tax Court reverses an STJ's credibility findings without having heard the witnesses personally, due process is violated. However, the verbatim adoption of the STJ's findings by the Tax Court would fully

comport with even Kanter's interpretation of *Raddatz*'s due process requirements.

But I agree with Kanter that when the Tax Court "agrees with and adopts the opinion of the Special Trial Judge," it does not mean that the Tax Court opinion is the verbatim reproduction of the original STJ's report. Kanter argues that the Tax Court routinely reviews and alters STJ reports through an internal process that is concealed in published Tax Court opinions by the language, "agrees with and adopts." Kanter presented two pieces of evidence to support his claim: 1) Kanter's attorney allegedly was told informally by Tax Court Judge Julian Jacobs and Chief Special Trial Judge Peter J. Panuthos that the credibility findings of Special Trial Judge Couvillion on fraud were reversed by Tax Court Judge Dawson;[1] and 2) there exists not a single Tax Court decision since the adoption of current Rule 183 where a Tax Court Judge has purported to modify or reverse a finding of a Special Trial Judge.

What Kanter alleges happened in the present case, and what commonly occurs in the Tax Court, is that a Tax Court judge takes the STJ's report (which had been filed with the Chief Judge pursuant to Rule 183) and works together with the STJ to edit it. From this process emerges a final report that may or may not bear any resemblance to the original report, but that still may be called the STJ's "opinion" (but not the STJ's "report") if the STJ agrees to subscribe to it. This modified report is then "adopted" by the Tax Court judge and filed as the Tax Court opinion. This is the reason, Kanter

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[1] Kanter's attorney revealed the names of the judges in question when asked at oral argument. The original declaration of Kanter's attorney did not name the Tax Court judges who allegedly made these statements concerning the alteration of the STJ's report. *Declaration of Attorney Randall G. Dick*, App. at 250-52.

argues, that, in the 880-plus Tax Court decisions since 1983 that I could find that involved an STJ report, the Tax Court judge purported to agree with and adopt the opinion of the STJ in *every* instance. Never, in any instance since the adoption of the current Rule 183 that I could find, has a Tax Court judge *not* agreed with and adopted the STJ's opinion.

I find this extraordinary unanimity telling. It is difficult to believe that over the course of nineteen years (since the amendments giving rise to current Rule 183), not a single Tax Court judge (and there are 19 of them, 26 U.S.C. § 7443(a)) has ever disagreed with a single original finding of any STJ (and there are about 20 of them). I say with confidence that this degree of unanimity is not only unusual, but impossible in a system of arms-length appellate style review involving 39 independent individuals. I believe that it is highly likely, therefore, that there is some kind of collaborative process involved in the path from STJ report to Tax Court decision. I draw support in this conclusion from the fact that neither the Commissioner nor the Tax Court has ever settled this issue by unambiguously stating otherwise, despite opportunities to do so. Notably, at oral arguments on the present case the Commissioner did not dispute Kanter's contention that the STJ's report undergoes some kind of revision during the process of "adoption" by the Tax Court. And in his brief the Commissioner is very careful in stating that the Tax Court adopted the "*opinion* of the [STJ]." Resp. Br. at 111 (emphasis added). And the Commissioner is just as careful in never stating that the Tax Court adopted the STJ's "*report*." This care mirrors the Tax Court's own language in its refusal to release the STJ's report to Kanter.

I believe that the record supports the notion that the Tax Court engages in a quasi-collaborative process of review of the STJ's report from which a new and frequently different STJ's opinion emerges to be adopted and agreed with by the Tax Court. If my understanding is correct, there are two

"STJ's reports" in many, if not most (or even all), Tax Court cases – the original "report" filed under Rule 183 with the Chief Judge of the Tax Court, which is solely the work product of the STJ (and which represented the STJ's views at the end of trial) and the later "opinion" of the STJ, which is a collaborative effort, but which the Tax Court then "agrees with and adopts" as the opinion of the Tax Court. In any event, I do not claim to know the degree to which the STJ's original filed report in the present case was altered, and I do not take as determinative of that fact the declaration of Kanter's attorney regarding his conversations with Tax Court personnel. So, given this interpretation of the Tax Court's procedure, I want to take a closer look at Kanter's argument.

Kanter's argument wraps a number of different issues into one request for the STJ's report. First, whether or not the Tax Court's procedure denying access to the STJ's report violates its own Rule 183. Second, whether the Tax Court's procedure violates other law, including the Internal Revenue Code ("IRC"). Third, whether the Tax Court's procedure violates due process protections. Finally, and most importantly, whether Kanter's due process rights on appellate review by this court are violated when we undertake review of the Tax Court's decision without the context of the STJ's original report with respect to credibility findings.

1. Does the Tax Court's procedure violate Tax Court Rule 183?

I agree with the majority's determination that Rule 183 imposes no requirement of disclosure or of clearly erroneous deference upon the Tax Court. However, I think some additional discussion of the evolution of Rule 183 into its current form, and why the current rule does not compel production of the STJ's report nor require any particular deference to the STJ's report, would be very informative. Kanter points us to *Stone v. Commissioner*, 865 F.2d 342 (D.C. Cir. 1989), where the Court of Appeals for the District of Columbia Cir-

cuit found that an STJ's findings should be reviewed by the Tax Court under a clearly erroneous standard. *Id.* at 347. Under a prior version of the Tax Court's rules (pre-1983 and which governed the case before the *Stone* court), the STJ's report was served on each party and each party had an opportunity to file objections to the report's findings. *See* Tax Court Rule 182(b), (c), 60 T.C. 1149, (1973). The *Stone* court's finding that the STJ's report was owed deference followed from the Tax Court rules, Rule 182(d) at the time, which stated that "[d]ue regard shall be given to the circumstance that the [STJ] had the opportunity to evaluate the credibility of witnesses; and the findings of fact recommended by the [STJ] shall be presumed to be correct." Tax Court Rule 182(d), 60 T.C. 1150, (1973). The explanatory notes to this rule prescribed that, in regard to the "special weight" to be given the STJ's findings, one should look to Court of Claims Rule 147(b). *Id.* The *Stone* court found this prescription particularly instructive because Rule 182(d)'s language was lifted practically verbatim from Court of Claims Rule 147(b). *Stone*, 865 F.2d at 345. At the time that the language of Court of Claims Rule 147(b) had been adopted for the Tax Court's rules, the Court of Claims interpreted that language to require review of the findings of its version of an STJ's report under a clearly erroneous standard. *See, e.g., Elmers v. United States*, 172 Ct. Cl. 226, 232 (1965). The *Stone* court found that the language of the rule, the rule's command to look to the Court of Claims and the Court of Claims' use of a clearly erroneous standard of review required the use of such a standard in the Tax Court's review of STJ findings. *Stone*, 865 F.2d at 347. However, the *Stone* court went on to note that

> The Tax Court is of course free to make its own rules determining the relation between it and its Special Trial Judges. Moreover, we assume that the Tax Court's construction of its own rules enjoys the deference, on review

> in this court, enjoyed by an administrative agency interpreting its own regulations.

Id. The Tax Court did exactly that – changed its rules.[2] In 1983, the Tax Court amended and redesignated the rule in

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[2] I have been unable to discover what, if any, formal documented procedure accompanies the adoption, amendment or repeal of a Tax Court rule. There does not exist, I believe, any written description of the process that is available in public records. Informal conversations with a Deputy Clerk of the Tax Court and the Tax Court's library have indicated that some section of the Tax Court comprises a rules committee that periodically issues rules and rule changes. There is some indication from these informal conversations and my research that proposed rules may be circulated to members of the tax bar for comment. *See, e.g., ABA Members Suggest Modifications to Proposed Amendments of Tax Court Rules*, 97 Tax Notes Today 167-25 (August 28, 1997). But there is no such requirement within the IRC or the Tax Court's rules. Like the process by which an STJ's report is composed and then withheld, I find this rulemaking procedure oddly out of sync with prevailing practices in other areas of the law. *Compare* 28 U.S.C. § 2071(b) ("Any rule prescribed by a court, other than the Supreme Court, under subsection (a) shall be prescribed only after giving appropriate public notice and an opportunity for comment.") *and* Fed. R. App. P. 47(a)(1) ("Each court of appeals acting by a majority of its judges in regular active service may, after giving appropriate public notice and opportunity for comment, make and amend rules governing its practice.") *with* 26 U.S.C. § 7453 ("[T]he proceedings of the Tax Court and its divisions shall be conducted in accordance with such rules of practice and procedure (other than rules of evidence) as the Tax Court may prescribe.") *and* Tax Court Rule 1(a) ("Where in any instance there is no applicable rule of procedure, the Court or the Judge before whom the matter is pending may prescribe the procedure, giving particular weight to the Federal Rules of Civil Procedure to the extent that they are suitably adaptable to govern the matter at hand.").

question, adopting its current form as Rule 183,[3] and noted that "[t]he prior provisions for service of the [STJ]'s report on each party and for the filing of exceptions to that report have been deleted."[4] 81 T.C. 1070, (1983). The Tax Court has never documented any explanation of why this amendment was undertaken. The Tax Court's power to prescribe its own rules of procedure is undisputed. 26 U.S.C. § 7453. And although the Tax Court is no longer an executive agency, *see Freytag v. Commissioner*, 501 U.S. 868, 887-88 (1991) (noting that in 1969 Congress removed the Tax Court from the realm of executive agencies and made it an Article I court), it is clear, and Kanter does not dispute, that the Tax Court's interpretation of its own rules of procedure receives a great deal of deference. Therefore, the 1983 amendment to

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[3] Current Tax Court Rule 183(c) provides:

> Action on the Report: The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions. Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct.

[4] One interesting detail involves the timing of the *Stone* decision and the change in current Rule 183. *Stone* involved events in the 1960s and a Tax Court trial in the 1970s (all events before the 1983 amendment of Rule 183), but the court of appeals decision is from 1989, well after the amendment. So, although the court was dealing with a case where the STJ's report was part of the record, it made the noted comment concerning the Tax Court's ability to amend the Tax Court rules at a time when that court had already done so. But the court of appeals decision made no mention of that amendment.

the Tax Court rules had the effect of no longer requiring that parties (or the general public or a reviewing court, for that matter) have access to the STJ's report.

Kanter notes, however, that the language of the earlier rule that prompted the clearly erroneous standard in *Stone* remains unchanged. The Tax Court judge still "shall" give "[d]ue regard" to the fact that the STJ had the opportunity to hear and evaluate the credibility of the witnesses, and the STJ's recommended findings of fact still "shall be presumed to be correct." Tax Court Rule 183(c). This language, according to Kanter, still commands the Tax Court judge to whom the STJ's report is submitted to adopt the STJ's findings unless the findings are clearly erroneous.[5] And there certainly appears to be some consensus in the literature that the Rule still embodies a clear error standard. *See, e.g.*, 35 Am. Jur. 2d Fed. Tax Enforcement § 905 (2002) ("The Tax Court is required to review a special trial judge's factual findings according to the clearly erroneous standard, and cannot overturn a special trial judge's ruling on the basis that the Tax Court finds the testimony credited by the trial judge to be unbelievable."); 20A Federal Procedure, L.Ed., Internal Revenue § 48:1274 (2000) (same); *but see Tax Court Litigation*, 630-2nd Tax Mgmt. Portfolio at A-49 n.599 (1997) ("The D.C. Circuit (but not the Tax Court) has taken the position that the level of deference is to review the Special Trial Judge's draft opinion on a 'clearly erroneous' standard."). However, I agree with the majority's conclusion that this is no longer the case, and I have nothing additional to add to its reasoning on the matter.

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[5] The *Stone* court, in fact, stated in its interpretation of the due regard and presumed correct language, that "until the [tax] court adopts new language, it must hew to the meaning of what it has said." *Stone*, 865 F.2d at 347.

Therefore, like the majority, I also do not believe that Tax Court Rule 183 requires an STJ's report to be reviewed under a clearly erroneous standard, nor that Rule 183 is violated by a quasi-collaborative process of revision of an STJ's report, nor that the Rule requires the production of the report. In spite of this I must again note how remarkable it is that not only is the Tax Court unique in the opacity of its process, but it has arrived at this opaque process by abandoning a transparent process – an evolution completely counter to the trend towards transparency in analogous areas of the law. *See, e.g.*, Elena Kagan, *Presidential Administration*, 114 HARV. L. REV. 2245, 2331-32 (2001) (describing new theory of administrative control in which author notes that transparency is a core value of administrative procedure). There is no public indication why the Tax Court rules and procedures were changed in 1983 to the current system that disadvantages those appealing Tax Court decisions. And, of course, an appellate-style procedure such as that typical in all other areas of federal administrative adjudication would facilitate challenges, whether made by the taxpayer or by the Commissioner. The previous procedure may well have been abrogated for exactly this reason.

2. Is the Tax Court's procedure otherwise unlawful?

The majority quite ably and clearly outlines why existing rules and statutes do not appear to *compel* inclusion of the STJ's report in the record on appeal. In doing so, the majority places significant weight on the Commissioner's argument analogizing the STJ-Tax Court judge relationship to the division-Tax Court relationship governed by 26 U.S.C. § 7460, in which a division's preliminary report is never made public if the Tax Court reviews the case and issues its own opinion. Before moving on to the meatier due process issues, I want to note that this analogy, however, overlooks some important considerations. First, a division whose report is reviewed by the Tax Court has the opportunity to file a dissent from the

Tax Court's final decision and place in that dissent any of its objections – objections that could, in theory, include the division's overruled findings that were contained in its original report. Thus, those original findings can be made public, albeit in a roundabout manner, if the division wants them to be. An STJ's original report is never made public.

Second, § 7460 differs significantly from Rule 183 in that it does not require "due regard" for the fact that the division has heard witnesses and evaluated credibility (perhaps because the division may not have been the adjudicator who heard the witnesses), nor does § 7460 require any presumption that the division's report is correct. In contrast, Rule 183 requires both due regard and a presumption of correctness for the STJ's report. Therefore, to the extent that the Tax Court's final opinion must, under Rule 183, accord some kind of respect to the STJ's original findings, the STJ's original report has some ongoing significance, whereas the division's report is of no consequence in the formulation (or appellate review) of the Tax Court's opinion.

Third, since the division may not have conducted the trial nor heard the witnesses, a policy of deference to such an adjudicator would not necessarily be appropriate. By contrast, an STJ is always the person who hears witnesses and, for that reason, is an adjudicator entitled to deference. Again, this raises the significance of the original STJ's report to the ultimate adjudication and review of the case in a way not present with a division's report.

And finally, the relationship between a division and the Tax Court is far different from the relationship between an STJ and the Tax Court. Tax Court judges are all, essentially, equal. They are presidentially appointed for statutorily mandated 15 year terms, and they each have an equal vote in the business of the Tax Court. 26 U.S.C. §§ 7443, 7444. An STJ is appointed at the discretion of the Chief Judge and has no statutorily mandated term of office. 26 U.S.C. § 7443A.

Congress has authorized specific and limited means for removing a Tax Court judge from office: "Judges of the Tax Court may be removed by the President, after notice and opportunity for public hearing, for inefficiency, neglect of duty, or malfeasance in office, but for no other cause." 26 U.S.C. § 7443(f). There is no such statutory protection for STJs. Ultimately, keeping a division's preliminary report secret appears less problematic given the division's almost unfettered ability to make its wishes clearly known in the final opinion without concern for job security or reprisal. However, an STJ serves at the discretion of the Tax Court, and his or her judicial independence is therefore quite circumscribed. Only by allowing access to the original STJ's report can the Tax Court insulate itself from the perception that an STJ's "findings" are arbitrarily malleable at the discretion of the Tax Court.[6]

In addition, there are other provisions of the Internal Revenue Code that, at the very least, show that Congress did

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[6] I am not suggesting that, in this case or in general, the judges of the Tax Court coerce or exert undue influence over STJs. The judicial independence of finders of fact, however, is a structural principle. The statutes and Tax Court Rules establishing and utilizing STJs lack the structure of judicial independence we find in, for example, our Article III courts. One way of imposing a structural modicum of judicial independence on the Tax Court would be through transparency and judicial review – providing access to the STJ's original report would allow for judicial independence without compromising the procedures of the Tax Court. This is the same procedure prescribed by the Administrative Procedure Act, which requires the report of the ALJ who heard the witnesses to be prepared and filed for public enlightenment. To describe the STJ system and lament its lack of structured judicial independence does not suggest that I am impugning the integrity of the distinguished members of the Tax Court. And this dissent should certainly not be interpreted in that way.

not demonstrate a clear intent to keep STJ reports secret – unlike the clear intent to keep division reports private that is shown in § 7460. 26 U.S.C. § 7459(b) states that the "Tax Court shall report in writing all its findings of fact, opinions, and memorandum opinions." Additionally, 26 U.S.C. § 7461(a) states that "all reports of the Tax Court * * * shall be public records," and 26 U.S.C. § 7462 states that the "Tax Court shall provide for the publication of its reports at the Government Printing Office in such form and manner as may be best adapted for public information and use * * *." While the majority is correct that there are no rules or statutory sections that specifically *require* that the initial report of the STJ be made public, there are, by the same token, no sections that *forbid* that the report be made public – in contrast to § 7460's clear intent to keep private a division report that is reviewed by the full Tax Court. And §§ 7459, 7461 and 7462 appear to establish a strong presumption in the IRC in favor of public dissemination of Tax Court documents that, apparently, could easily apply to the STJ's report. Only a formalistic interpretation by the Tax Court that the STJ's report is not a "report of the Tax Court" allows it to avoid such a presumption.

3. Does the Tax Court's procedure violate due process?

Due process requires that Kanter have been afforded a fair hearing before he is deprived of property. *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976). Notice and an opportunity to be heard are the hallmarks of a fair hearing. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 313 (1950). The Supreme Court in *Raddatz* reiterated the three part test announced in *Mathews* for evaluating due process protections:

> [T]hree factors should be considered in determining whether the flexible concepts of due process have been satisfied: (a) the private interests implicated; (b) the risk

> of an erroneous determination by reason of the process accorded and the probable value of added procedural safeguards; and (c) the public interest and administrative burdens, including costs that the additional procedures would involve.

Raddatz, 447 U.S. at 677 (citing *Mathews*, 424 U.S. at 335). In the context of the present case, one would need to determine whether a quasi-collaborative process wherein the ultimate finder of fact, who has not heard the witnesses herself, can amend, revise or reverse the preliminary findings of the person who actually heard the witnesses (and never reveal those preliminary findings) without running afoul of the Fifth Amendment. This comprises two separate questions: (1) must the Tax Court review the STJ's findings with a formal degree of deference (such as clear error); and (2) must the Tax Court itself hear witnesses to determine issues of credibility before reversing the STJ?[7]

As *Raddatz* and *Universal Camera* make clear, at one end of the due process spectrum – the general administrative law context – due process does not require that the ultimate fact finder be constrained by a formal degree of deference to the original hearing officer. Nor must that fact finder rehear wit-

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[7] Kanter has separated these two oft intertwined concepts in his arguments when he alleges that 1) the Tax Court owes the STJ a formal degree of deference and 2) the Tax Court cannot change the STJ's findings without having heard the witnesses. Once it is determined that, under the Fifth Amendment, the Tax Court can act as an original fact finder and determine facts *de novo*, then one must ask whether the method of conducting that factual determination can be done based on a transcript of witness testimony or only by actually hearing the witnesses first hand. The first question may or may not be a pure procedural due process question, but its answer is clear and it serves to frame the more difficult second question for analysis.

nesses before making findings, whether or not the fact finder reverses the original hearing officer's findings. *See id.* at 680 ("Generally, the ultimate factfinder in administrative proceedings is a commission or board, and such trier has not heard the witnesses testify * * *. While the commission or board * * * may defer to the findings of a hearing officer, that is not compelled."); *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 492-94 (1951); *see also* 5 U.S.C. § 557(b) ("On appeal from or review of the initial decision, the agency has all the powers which it would have in making the initial d cision * * *."); Kenneth Culp Davis & Richard J. Pierce, Jr., *Administrative Law* § 8.6, at 396 (3d ed.1994) (noting that the command of *Morgan v. United States*, 298 U.S. 468, 481 (1936), that "the one who decides must hear," "did not mean that an agency head who decides must listen to the witnesses testify").

At the other end of the due process spectrum lies the criminal procedure context, where due process protections are the most demanding. First, regarding deference, the Supreme Court in *Raddatz* did not directly address the issue, but the Federal Magistrates Act under review required the district court to conduct a *de novo* review of the magistrate judge's findings, and the Court took no issue with that standard of review, even for credibility findings. This parallels the administrative context, and demonstrates, I believe, that along the full continuum of due process concerns framed by *Raddatz* and *Universal Camera*, there is no per se due process violation when the ultimate finder of fact reviews preliminary findings *de novo*. Therefore, I agree with the majority that the Fifth Amendment does not require that the Tax Court review STJ findings using any particular degree of deference. This means also that there is no constitutional requirement that the Tax Court use an appellate-style review of its STJs' reports. In this respect, the quasi-collaborative model adopted by the Tax Court is permissible.

Second, what about the rehearing of witnesses in a criminal procedure context? While, under the *Mathews* analysis, the interests of a criminal defendant in a suppression hearing are not as significant as they may be in a full criminal trial, they are significant enough that the Supreme Court issued a warning that "serious questions" existed in the situation wherein a district court judge reversed a magistrate judge's dispositive credibility findings without hearing the witness herself. *Raddatz*, 447 U.S. at 681 n.7.[8] Several of our sister circuits have found that these "serious questions" have a single answer: a district court judge cannot reverse a magistrate's credibility findings without hearing the witness at issue. *See, e.g., United States v. Cofield*, 272 F.3d 1303, 1305-06 (11th Cir. 2001); *Hill v. Beyer*, 62 F.3d 474, 482 (3d Cir. 1995); *United States v. Rosa*, 11 F.3d 315, 328-29 (2d Cir. 1993); *In re Hipp, Inc.*, 895 F.2d 1503, 1519-21 (5th Cir. 1990); *see also United States v. Mejia*, 69 F.3d 309, 316-20 (9th Cir. 1995) (finding that footnote 7 of *Raddatz* applied to a suppression hearing where the judge making the ruling received *no* findings on credibility from the judge who heard the witnesses' testimony; the court ruled it was a due process violation to make such a ruling without having heard the witnesses).

However, as the Commissioner points out, the interests in *Raddatz* were more significant because that case involved an aspect of a criminal trial, and the proceedings before the Tax Court are eminently civil. Under the *Mathews* framework,

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[8] Footnote 7 in *Raddatz* states in relevant part:

> The issue is not before us, but we assume it is unlikely that a district judge would *reject* a magistrate's proposed findings on credibility when those findings are dispositive and substitute the judge's own appraisal; to do so without seeing and hearing the witness or witnesses whose credibility is in question could well give rise to serious questions which we do not reach.

the private concerns involved in a civil proceeding are not entitled to the same level of due process protection as the concerns in a criminal proceeding, just as *Raddatz* notes that within a criminal proceeding a suppression hearing embodies a lower interest than other aspects of a criminal trial. *See Bristol-Myers Squibb Co. v. McNeil-P.P.C., Inc.*, 973 F.2d 1033, 1045 (2d Cir. 1992) ("Moreover, we have indicated that the *Raddatz dicta* may be inapplicable outside the criminal context * * *.").

While it is not an easy issue, I believe that the interests at stake in a civil tax court proceeding do not rise to the level addressed in *Raddatz*, and are more analogous to the interests involved in an administrative adjudication. There certainly is some cause for concern that a finding of credibility on a "cold record" as voluminous as the one before us here increases the chance of an erroneous determination, but I do not believe that that possibility in this kind of civil proceeding is as high, nor the costs as great, as would be the case in a criminal milieu. Additionally, I would note that the only fully responsive remedy would be to require the Tax Court itself to rehear the witnesses whose credibility was at issue. Under the third prong of the *Mathews* test this added procedure would probably be an enormous burden and impose a prohibitive cost. The added value of such procedure under the second prong of *Mathews* seems insubstantial, especially given that the quasi-collaborative model can provide the Tax Court with ongoing access to the thoughts and impressions of the STJ who actually heard the witnesses. Additionally, I believe that one possible advantage of the quasi-collaborative process (over standard appellate-style review) might be an opportunity for the STJ to have additional input into the decision making process beyond her original report.[9] This oppor-

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[9] However, I reiterate that the judicial independence of the STJ, who serves at the discretion of the Tax Court, is suspect. The

tunity should do something to minimize the risk of an erroneous determination.

Hence, the *dictum* in *Raddatz* does not persuade me that the reversal of an STJ's findings by the Tax Court following a quasi-collaborative procedure violates due process. In a real sense, my writing to this point has been more concurrence than dissent. But I feel it very important to navigate these areas of agreement in order to properly prepare for the pivotal area of disagreement, where I part ways with the majority.

4. Does appellate review of the Tax Court's findings without access to the STJ's report violate due process?

There is another stage of procedure involved here (and a key one from my perspective) that requires due process analysis – appellate review of the Tax Court's decision. Whether or not the STJ's report is made available to the parties for comment before the Tax Court issues its findings, and whether or not the Tax Court can reverse the STJ's purportedly dispositive credibility findings without having heard the relevant witnesses, the question still remains whether or not the due process rights of the parties before *this court* are violated when we have no opportunity to review the Tax Court's

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structure of the STJ process does nothing to expressly preserve the voice or influence of an STJ in the formulation of the final opinion. Therefore, I do not accord a great deal of weight to the influence of the STJ over the Tax Court's review of the STJ's report. In this way I differ not only from the majority, but also from the conclusion of the Eleventh Circuit, which analogizes a Tax Court judge's conferring with an STJ to members of an appellate panel conferring with one another. *See Ballard*, 321 F.3d at 1043. In the Tax Court situation, only one of the conferees has attended the trial and heard the witnesses and the conferees are not of equal rank nor do they possess an equal degree of judicial independence.

factual findings for clear error in light of the STJ's initial report. *See Evitts v. Lucey*, 469 U.S. 387, 393 (1985) (there is no constitutional right to appeal, but once a right of appeal is created, it must comport with due process to be meaningful and effective). This question distinguishes the issue whether the Tax Court's procedures are intrinsically unfair (which neither I nor the majority believe is true) from the issue whether the Tax Court's procedures are unreviewable (on which the majority and I disagree).[10] The essential difference is that the Tax Court has the report; we do not.

Our review of the Tax Court is governed by the same standards as those governing our review of a district court's civil bench trial; this means that legal conclusions are reviewed *de novo* and findings of fact are reviewed for clear error. *See* 26 U.S.C § 7482(a); *Pittman v. Commissioner*, 100 F.3d 1308, 1312-13 (1996). Obviously, we do not need access to the STJ's report to conduct meaningful *de novo* review of the Tax Court's legal conclusions. But clearly erroneous review involves deference to the conclusions of the fact finder – the Tax Court in the present case. This is a deference that the Supreme Court has attributed, in the case of credibility, to the fact finder's first-hand observations of the witnesses in question.

> [A] finding is "clearly erroneous" when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed.

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[10] This question does not depend upon the Tax Court's being required to give some level of formal deference to the STJ's report. Although the question before us would be much easier to answer if such a requirement existed, I am asking the more fundamental question whether our clear error review of the Tax Court's findings can be meaningful without the context of the STJ's report to inform that review.

* * *

> When findings are based on determinations regarding the credibility of witnesses, [the clearly erroneous standard] demands even greater deference to the trial court's findings; for only the trial judge can be aware of the variations in demeanor and tone of voice that bear so heavily on the listener's understanding of and belief in what is said.

Anderson v. City of Bessemer City, N.C., 470 U.S. 564, 573, 575 (1985) (citations omitted). Thus, it is integral to the standard of clear error review that there be deference to the credibility findings of the official who has actually heard the witnesses. Although the Supreme Court in *Anderson* was discussing the deference due a finder of fact who has, himself, heard the witnesses, I think the Court's command is also instructive in two ways. First, on its face *Anderson* instructs that on issues of credibility the opportunity to hear witnesses is significant in a clear error context. Second, *Anderson* informs that context by impliedly undermining the reliability of findings that reverse the credibility determinations of an official who has actually heard the witnesses. If we are to give "even greater deference" to the findings of a judge who has heard the witness whose credibility is at stake, we must inevitably give less deference to the judge who subsequently reverses those findings.

I find major support for this line of thinking in the administrative law arena.[11] In the administrative context, the Ad-

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[11] Most review of administrative agency determinations or adjudications is done under the "substantial evidence" standard. The clear error standard, which we apply to the review of district court as well as Tax Court factual findings, is virtually indistinguishable from the substantial evidence standard. *See School District of Wisconsin Dells v. Z.S.*, 295 F.3d 671, 674 (7th Cir. 2002) ("'[T]he difference [between clear error and substantial evidence] is a subtle

ministrative Procedure Act requires that a reviewing court examine an agency determination based on a record that includes any preliminary findings from the hearing officer (like an Administrative Law Judge (ALJ)).[12] 5 U.S.C. §§ 557(b), 706. When a reviewing court reviews agency findings on credibility for substantial evidence, it is strongly influenced by the preliminary findings of the ALJ who actually heard the witnesses – influence that becomes even more significant when an agency has reversed those preliminary credibility findings. *See Kopack v. NLRB*, 668 F.2d 946, 953 (7th Cir. 1982) ("One must attribute significant weight to an ALJ's findings based on demeanor because neither the [NLRB] nor the reviewing court has the opportunity similarly to observe the testifying witnesses."); *Moore v. Ross*, 687 F.2d 604, 609 (2d Cir. 1982) ("Accordingly, reviewing courts have often found federal decisions unsupported by substantial evidence when they hinge on assessments of credibility contrary to those made by the ALJ who heard the witnesses."); *Ward v. NLRB*, 462 F.2d 8, 12 (5th Cir. 1972) ("The preeminence of the Examiner's conclusions regarding testimonial probity does not amount to an inflexible rule that either the Board or

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one – so fine that * * * we have failed to uncover a single instance in which a reviewing court conceded that the use of one standard rather than the other would in fact have produced a different outcome.'"), quoting *Dickinson v. Zurko*, 527 U.S. 150, 162-63 (1999); *see also Tripp v. Commissioner*, 337 F.2d 432, 434 (7th Cir. 1964) (using both "clear error" and "substantial evidence" in reference to review of Tax Court's findings of fact). Therefore, I look for guidance to the administrative law context, in which reviewing courts examine administrative agency determinations (including adjudications).

[12] And again, in the administrative context an agency can make factual findings *de novo*, regardless of any preliminary findings, much as the Commissioner claims the Tax Court can do with respect to an STJ's report.

a reviewing court must invariably defer to his decision, thereby effectively nullifying either administrative or judicial review. But when the Board second-guesses the Examiner and gives credence to testimony which he has found – either expressly or by implication – to be inherently untrustworthy, the substantiality of that evidence is tenuous at best.").

The Supreme Court in *Universal Camera* best summarized the philosophy behind this process: "We intend only to recognize that evidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion." 340 U.S. at 496. This is never more the case than when the issue is one of credibility. As the Supreme Court said in *Raddatz*, it is within the context of credibility that findings based on a "cold record" are most suspect if they differ from the findings of the one who actually heard the witnesses in question.

> To be sure, courts must always be sensitive to the problems of making credibility determinations on the cold record. More than 100 years ago, Lord Coleridge stated the view of the Privy Counsel that a retrial should not be conducted by reading the notes of the witnesses' prior testimony:
>
> "The most careful note must often fail to convey the evidence fully in some of its most important elements * * *. It cannot give the look or manner of the witness: his hesitation, his doubts, his variations of language, his confidence or precipitancy, his calmness or consideration; * * * the dead body of the evidence, without its spirit; which is supplied, when given openly and orally, by the ear and eye of those who receive it." *Queen v. Bertrand*, 4 Moo. P.C.N.S. 460, 481, 16 Eng. Rep. 391, 399 (1867).

Raddatz, 447 U.S. at 679-80. And unlike *Raddatz*, in the present case we are dealing with a full trial by a judge on the merits, albeit a civil trial (on the "quasi-criminal" issue of fraud), and not an ancillary motion to suppress. Additionally, the present case was inordinately long and complicated, and the resolution of issues required the synthesis of multiple witnesses' testimony that was separated by days or even weeks (and by hundreds or thousands of pages in the transcript). Whatever advantage is to be gained by a first-hand observation of witnesses is multiplied exponentially when the trial is so long and the transcript so voluminous. The detailed interconnection of the credibility of different witnesses on different factual issues makes the accumulated impressions of the presiding officer irreplaceable. I can think of no single item of more significance in evaluating a Tax Court's decision on fraud than the unfiltered findings of the STJ who stood watch over the trial.

The difficulty comes in determining how and when this concern rises to the constitutional level of due process. No court of which I am aware has ever considered the ramifications of an agency's swallowing and refusing to regurgitate a preliminary factual finding in the manner done by the Tax Court here. The reason for this is clear: the Administrative Procedure Act requires the publication of such findings for executive agencies. And no court that I could find has ever discussed the availability of preliminary findings as being related to due process protections. Only *Universal Camera*'s *dicta* on the value of the preliminary findings comes close, and the Supreme Court there clearly based its decision in the language of the Administrative Procedure Act.

However, under the three-part test of *Mathews* and *Raddatz*, I think it not unreasonable to invoke due process in this context at the appellate court level of review. Under the first prong of *Mathews*, I note again that the quasi-criminal nature of fraud is a more significant private interest than a simple

civil determination, but not as weighty an interest as in the criminal suppression hearing in *Raddatz*. Under the second prong, however, I believe the risk of error here is greater and the value of the added procedural safeguard (the STJ's report) is higher in this context. Without the STJ's report we would be reviewing deferentially a credibility finding made by the Tax Court based on a cold record (albeit with the theoretical collaboration of the STJ who actually heard the witnesses) based on our own analysis of that same cold record. The precedents noted in the administrative context (as well as *Universal Camera*) clearly demonstrate how valuable preliminary findings are for review in cases like the present one. Under the *Mathews* test's third prong, the added cost and administrative burden in this instance is *de minimis* – publishing the STJ's report. On balance, I believe strongly that the absence of the STJ's report in the record for our consideration of the Tax Court's decision creates legitimate due process concerns with respect to our review.

What throws a real analytical monkey wrench into all of this is that the result of the collaborative process in the Tax Court is an opinion that, allegedly, represents the "opinion" of the STJ (but not, I repeat, the "report" of the STJ). What this could mean is that the collaboration of the Tax Court with the STJ has produced an opinion that represents the revised and true legal opinions and findings of the STJ. The original report, by necessity therefore, would no longer be a valid statement of the STJ's findings inasmuch as it differed from the final opinion. Therefore, to the extent that due process is concerned with the changes that the Tax Court makes to the findings contained in the STJ's report (which would represent points of disagreement between the Tax Court and the STJ), those concerns are balanced by the fact that the STJ does not actually disagree with those changes and, in fact, has certified to their correctness by signing off on the opinion. I could, in the best of all possible worlds,

liken this to a learning process whereby the original impressions of the STJ are tempered through the collaborative process with the Tax Court, and, I would assume, the Tax Court's opinions would be molded and informed by the first-hand impressions of the STJ. Whatever limitations on review this process entails would be balanced by the fact that the STJ does not still hold opinions or findings in conflict with those represented in the opinion. In such a world, it no longer seems so strange that every Tax Court case involving an STJ resulted in an opinion that agreed with and adopted the opinion of the STJ – the final opinion represents a compromise between the positions both of the Tax Court judge and of the STJ. (This view of things would still remain somewhat disingenuous because the Tax Court opinion's language clearly seeks to imply that the opinion represents the original report of the STJ.) I believe that this is, more or less, the position taken by the majority.

The obvious rejoinder to this utopian view of the Tax Court's process is to point out what I have already noted: the STJs are not equal to the Tax Court judges and it might be naive to assume that the STJs have an equal voice in the collaborative process that results in Tax Court opinions. The result is a system whereby the Tax Court maintains total discretionary control over the function of STJs but expects a reviewing court to simply accept at face value the declaration that the opinion is the opinion of the STJ. On the one hand, I certainly do not believe that the Tax Court is prevaricating and forcing STJs to cooperate under the express threat of unemployment. However, judicial independence in the context of due process is not a principle to be taken lightly, and its absence has consequences. The fact is that this entire process of the Tax Court appears designed to extract the efficiencies involved in designating cases to be heard by STJs without having to bear any of the procedural costs traditionally associated with this kind of adjunct decision-making (e.g., trans-

parency). I do not believe that the STJ's ultimate assent to the final opinion of the Tax Court is protection enough to the parties. The majority does.

Because I dissent, I do not have to articulate a final outcome, but merely note that I find a due process violation. However, the solution is simple in theory. The due process violation is avoided by interpreting 26 U.S.C. §§ 7459, 7461 and 7462 so as to require publication of the STJ's original report as a report of the Tax Court. *See Edward J. DeBartolo Corp. v. Florida Gulf Coast Bldg. & Const. Trades Council*, 485 U.S. 568, 575 (1988). This appeal would be stayed to allow the STJ's original report to be made part of the record. It is significant to summarize what I do not say here. I do not believe that due process requires that the parties be allowed to file objections to the STJ's report before the issuance of the Tax Court's opinion. Nor do I necessarily believe due process requires that the STJ's report be made public before the Tax Court issues its ultimate opinion. But by eventually making the STJ's report public (and part of the available record of the Tax Court on appeal), this court will have an opportunity to conduct meaningful appellate review. Further, this is a procedural result that may benefit all parties, including the Commissioner, not just petitioners like Kanter – Tax Court decisions can very easily reverse findings (credibility – related and otherwise) of STJs in a manner that is detrimental to the Commissioner as well as to a petitioner.

After all of these pages, what I find most interesting is that I believe the majority and I are in complete agreement on the central issue here – that the views of the STJ matter. When I say that, however, I look at the structure of the process under which the STJ's views can be discarded without leaving a trace and I find the glass half-empty. The majority sees the verbal formula ("agrees with and adopts") and finds the glass half-full. I do not believe that the concealment of the Tax Court's revision process behind that verbal formula

allows this court to conduct meaningful appellate review. I appear, at the moment at least, to be alone in that belief. Therefore, I respectfully dissent.[13]

---

[13] Although, again, I concur as to the part of the opinion concerning the appeal of Naomi Kanter.

United States Tax Court.

INVESTMENT RESEARCH ASSOCIATES, LTD., AND SUBSIDIARIES, ET AL.,
Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

Nos. 25875-90, 23178-91, 26918-92, 20211-91, 1984-92, 22884-93, 21555-91, 19314-92, 25981-93, 43966-85, 3456-88, 26251-90, 45273-86, 32103-88, 20219-91, 31301-87, 16421-90, 24002-91, 21616-91, 16164-92, 25976-93, 33557-87, 23743-92, 712-86, 30830-88, 7557-93, 1350-87, 27444-89.

Dec. 15, 1999.

MEMORANDUM FINDINGS OF FACT AND OPINION

DAWSON, J.

These consolidated cases were assigned to Special Trial Judge D. Irvin Couvillion pursuant to Rules 180, 181, and 183. The Court agrees with and adopts the opinion of the Special Trial Judge, which is set forth below.

OPINION OF THE SPECIAL TRIAL JUDGE

COUVILLION, Special Trial J.

In these consolidated cases, respondent determined deficiencies in petitioners' Federal income taxes, additions to tax, penalties, and increased interest, as follows:

[The balance of the 600-page opinion, reported at 78 T.C.M. (CCH) 951, is omitted at this time with the permission of the Clerk of Court.]

UNITED STATES TAX COURT
Washington, D.C. 20217

INVESTMENT RESEARCH ASSOCIATES, LTD., AND SUBSIDIARIES, ET AL.	)	
Petitioners,	)	
v.	)	
	) Docket Nos.	43966-85, 712-86, 45273-86, 1350-87, 31301-87, 33557-87, 3456-88, 30830-88, 32103-88, 27444-89, 16421-90, 25875-90, 26251-90, 20211-91, 20219-91, 21555-91, 21616-91, 23178-91, 24002-91, 1984-92, 16164-92, 19314-92, 23143-92, 26918-92, 7557-93, 22884-93, 25976-93, 25981-93.
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

ORDER

On August 22, 2000, petitioners filed a Motion for Reconsideration of the Court's Denial of Petitioners' Motion for Access to Original Special Trial Judge Report Prepared Under Rule 183(b) or, In The Alternative, for a New Trial. This is the third time petitioners have filed a motion seeking ac-

cess to "all reports, draft opinions, or similar documents prepared and delivered to the Court pursuant to Rule 183(b)". By Order dated April 26, 2000, the Court denied petitioners' motion in all respects setting forth its reasons. In that Order it was stated that the provisions of section 7443A(b)(4), Internal Revenue Code, and Rule 183, Tax Court Rules of Practice and Procedure, were followed by the Court. See *Freytag v. Commissioner*, 501 U.S. 868, 871-875 (1991), affg. 904 F.2d 1011, 1014-1015 (5th Cir. 1990). Section 7443A(b)(4) provides that the chief judge may assign to special trial judges "any other proceeding which the chief judge may designate, to be heard by the special trial judges of the court". Rule 183, first adopted effective January 16, 1984, provides as follows:

> **(a) Trial and Briefs:** A Special Trial Judge shall conduct the trial of any such case assigned for such purpose. After such trial, the parties shall submit their briefs in accordance with the provisions of Rule 151. Unless otherwise direct, no further briefs shall be filed.
>
> **(b) Special Trial Judge's Report:** After all the briefs have been filed by all the parties or the time for doing so has expired, the Special Trial Judge shall submit a report, including findings of fact and opinion, to the Chief Judge, and the Chief Judge will assign the case to a Judge or Division of the Court.
>
> **(c) Action on the Report:** The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions. Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact

recommended by the Special Trial Judge shall be presumed to be correct.

The Note to Rule 183 states:

"The prior provisions for service of the Special Trial Judge's report on each party and for the filing of exceptions to that report have been deleted". 81 T.C. at 1070. The reason for the Note was that procedures which existed before January 16, 1984, were changed by Rule 183.

The present procedures of Rule 183 were expressly approved by the Supreme Court in *Freytag v. Commissioner*, 501 U.S. at 874, where it is stated that special trial judges have the authority to *hear* cases and prepare *proposed* findings and opinions, but that they lack the authority to decide cases under section 7443A(b)(4) because that is "reserved exclusively for judges of the Tax Court".

Also in the Court's order dated April 26, 2000, we stated:

> Therefore, petitioners' motion requesting access to any internal Court documents, including any preliminary drafts of reports or opinions, documents, memorandums or notes by judges, special trial judges or employees of the Court, will be denied. In any event such materials are confidential and not subject to production because they relate to the internal deliberative processes of the Court.

On May 30, 2000, the Court denied petitioners' motion to place the original report of the Special Trial Judge under seal and made a part of the record so that it would be available to a court of appeals for review.

In the present motion seeking again access to "all reports, draft opinions or similar documents" prepared pursuant to Rule 183(b), Randall G. Dick, counsel for petitioners Investment Research Associates, Ltd., and Burton W. Kanter and Naomi R. Kanter, for the first time in the motion and in his declaration attached thereto, has made general assertions,

without specificity, that two or three judges of the Court informed him that an original report of Special Trial Judge Couvillion "concluded that payments made by the Five were not taxable to the individual Petitioners and that the fraud penalty was not applicable". Although Mr. Dick states in his declaration that some judges commented about the procedures involved in handling these cases, whatever may have been said to Mr. Dick is irrelevant and immaterial.

The only official Memorandum Findings of Fact and Opinion by the Court in these cases is T.C. Memo. 1999-407, filed on December 15, 1999, by Special Trial Judge Couvillion, reviewed and adopted by Judge Dawson, and reviewed and approved by former Chief Judge Cohen.

Judge Dawson states and Special Trial Judge Couvillion agrees, that, after a meticulous and time-consuming review of the complex record in these cases, Judge Dawson adopted the findings of fact and opinion of Special Trial Judge Couvillion, that Judge Dawson presumed the findings of fact recommended by Special Trial Judge Couvillion were correct, and that Judge Dawson gave due regard to the circumstance that Special Trial Judge Couvillion evaluated the credibility of witnesses.

Petitioners have requested that Judge Dawson recuse himself from further consideration of these cases. He declines to do so. Chief Judge Wells upon review of the motion and consideration of the matter concludes that there are no valid grounds for compelling Judge Dawson to recuse himself.

In the alternative, petitioners have moved that the Court order a new trial before a new Tax Court judge. Chief Judge Wells views this as a motion without sufficient grounds to support it. Therefore, a new trial before another judge of the Court will not be ordered. Once the decisions are entered, petitioners may appeal the decisions if they so choose.

Accordingly, it is

ORDERED that Petitioners' Motion for Reconsideration of the Court's Denial of Petitioners' Motion for access to Original Special Trial Judge Report Prepared Under Rule 183(b) Or, In The Alternative, For a New Trial is denied.

/s/ THOMAS B. WELLS
THOMAS B. WELLS
CHIEF JUDGE

/s/ HOWARD A. DAWSON, JR.
HOWARD A. DAWSON, JR.
JUDGE

/s/ D. IRVIN COUVILLION
D. IRVIN COUVILLION
SPECIAL TRIAL JUDGE

DATED: WASHINGTON, D.C.
AUGUST 30, 2000

UNITED STATES TAX COURT

INVESTMENT RESEARCH ASSOCIATES, LTD., AND SUBSIDIARIES, ET AL.	)	
Petitioners,	)	
v.	)	
	)	Docket Nos.
	)	43966-85, 712-86,
	)	45273-86, 1350-87,
	)	31301-87, 33557-87,
	)	3456-88, 30830-88,
	)	32103-88, 27444-89,
	)	16421-90, 25875-90,
	)	26251-90, 20211-91,
	)	20219-91, 21555-91,
	)	21616-91, 23178-91,
	)	24002-91, 1984-92,
	)	16164-92, 19314-92,
	)	23143-92, 26918-92,
	)	7557-93, 22884-93,
	)	25976-93, 25981-93.
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

U.S. TAX COURT

DENIED

MAY 30 2000

/s/ Howard A. Dawson, Jr.
JUDGE

PETITIONERS' MOTION TO PLACE ORIGINAL SPECIAL TRIAL JUDGE REPORT PREPARED PURSUANT TO RULE 183(B) UNDER SEAL AND MADE PART OF THE RECORD FOR REVIEW BY THE CIRCUIT COURT OF APPEALS

PETITIONERS MOVE, that the original report, or equivalent document, submitted by Special Trial Judge Couvillion pursuant to Rule 183(b) to the Chief Judge be placed under seal and made part of the record for review by the Circuit Court of Appeals.

IN SUPPORT THEREOF, petitioners respectfully show unto the Court:

1. On April 20, 2000, petitioners filed Petitioners' Motion for Access to Original Special Trial Judge Report Prepared Under Rule 183(b) and a supporting Memorandum of Points and Authorities seeking access to the original Special Trial Judge Report, or equivalent document, prepared pursuant to Rule 183(b). In the alternative, petitioners requested that a copy of the requested materials be made part of the record for review by the Circuit Court of Appeals.

2. By Order dated April 26, 2000, the Court denied Petitioners' Motion for Access to Original Special Trial Judge Report Prepared Under Rule 183(b) and denied petitioners request that a copy of the requested materials be made part of the record for review by the Circuit Court of Appeals.

3. Unless the original Special Trial Judge report, or equivalent document, is placed under seal for review by the. Circuit Court of Appeals, it will be impossible for the reviewing court to determine whether petitioners' rights under the Due Process Clause of the Fifth Amendment were violated.

4. Unless the original Special Trial Judge report, or equivalent document, is placed under seal for review by the

Circuit Court of Appeals, it will be impossible for the reviewing court to determine whether the Tax Court Judge to whom these cases were assigned. for review pursuant to Rule 183 applied the proper standard of review (clearly erroneous) before modifying the factual determinations of the Special Trial Judge.

5. Respondent objects to the granting of petitioner's motion.

WHEREFORE IT IS PRAYED, that this Motion be granted and that the original Special Trial Judge report, or equivalent document, be placed under seal and made part of the record herein for review by the Circuit Court of Appeals.

DATED: MAY 25, 2000.

RESPECTFULLY SUBMITTED.

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UNITED STATES TAX COURT
Washington, D.C. 20217

INVESTMENT RESEARCH ASSOCIATES, LTD., AND SUBSIDIARIES, ET AL.,	)	
Petitioners,	)	
v.	)	
	) Docket Nos.	43966-85, 712-86, 45273-86, 1350-87, 31301-87, 33557-87, 3456-88, 30830-88, 32103-88, 27444-89, 16421-90, 25875-90, 26251-90, 20211-91, 20219-91, 21555-91, 21616-91, 23178-91, 24002-91, 1984-92, 16164-92, 19314-92, 23143-92, 26918-92, 7557-93, 22884-93, 25976-93, 25981-93.
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

ORDER

On April 20, 2000, petitioners filed a document entitled Motion for Access to Original Special Trial Judge Report Prepared Under Rule 183(b) and a supporting Memorandum of Points and Authorities. The motion seeks access to "all reports, draft opinions or similar documents prepared and

delivered to the Court pursuant to Rule 183(b)". If the motion is denied, petitioners request that the Court certify the issue for an interlocutory appeal pursuant to Rule 193, Tax Court Rules of Practice and Procedure. In the alternative, petitioners have requested that "a copy of the requested materials be made part of the record herein for review by the Circuit Court of Appeals".

These consolidated cases were assigned by the Chief Judge to be heard by Special Trial Judge Couvillion pursuant to section 7443A(b)(4), Internal Revenue Code, and Rule 183(a). They were heard in Chicago, Illinois. After a lengthy trial, consisting of testimonial and voluminous documentary evidence, and the filing of briefs (totaling 4,768 pages with respect to 41 litigated issues), Special Trial Judge Couvillion submitted his report containing findings of fact and opinion pursuant to Rule 183(b), which ultimately became the Memorandum Findings of Fact and Opinion (T.C. Memo. 1999-407) filed on December 15, 1999.

In accordance with Rule 183(c), the Chief Judge referred the cases to Judge Dawson for review and, if approved, for adoption. In reviewing the Special Trial Judge's report, Judge Dawson gave due regard to the fact that Special Trial Judge Couvillion evaluated the credibility of witnesses, as reflected in the Memorandum Findings of Fact and Opinion (T.C. Memo. 1999-407), and he treated the findings of fact recommended by the Special Trial Judge as being presumptively correct.

The report of the Special Trial Judge, as adopted by Judge Dawson, was then submitted to and reviewed and approved by the Chief Judge, who directed that it be filed as the Court's Memorandum Findings of Fact and Opinion. Thus the provisions of section 7443A(b)(4) and Rule 183 were followed by the Court. See *Freytag v Commissioner*, 501 U.S. 868, 871-875 (1991), affg. 904 F.2d 1011, 1014-1015 (5th

Cir. 1990); *Erhard v. Commissioner*, 46 F.3d 1470, 1475-1476 (9th Cir. 1995), which involved identical procedures.

Contrary to petitioners' assertion, the procedures pertaining to United States magistrate judges under 28 U.S.C., Sec. 636(b)(1) in hearing nonjury civil cases are different from those governing special trial judges under section 7443A(b)(4), I.R.C. and Rule 183. In particular, consent of the parties is not required in cases heard by special trial judges; and there is no requirement under Rule 183 that the findings of fact and opinion of a special trial judge be served on the parties and made subject to objections before being assigned to a judge for review and adoption. The Supreme Court expressly stated in *Freytag v. Commissioner*, 501 U.S. at 874:

> Petitioners appear not to appreciate the distinction between the special trial judges' authority to hear cases and prepare proposed findings and opinions under subsection (b)(4) and their lack of authority actually to decide those cases, which is reserved exclusively for judges of the Tax Court.

Therefore, petitioners' motion requesting access to any internal Court documents, including any preliminary drafts of reports or opinions, documents, memorandums or notes by judges, special trial judges or employees of the Court, will be denied. In any event such materials are confidential and not subject to production because they relate to the internal deliberative processes of the Court. Cf. Sec. 7460(b); *Estate of Varian v. Commissioner*, 396 F.2d 753, 754-755, n.2 (9th Cir. 1968), affg. 47 T.C. 34 (1966); *Heim v. Commissioner*, 251 F.2d 44, 48 (8th Cir. 1958), affg. 27 T.C. 270 (1956).

Petitioners next contend that the denial of their motion for production of documents requires the Court to certify the issue for an interlocutory appeal pursuant to section

7482(a)(2), I.R.C., and Rule 193, Tax Court Rules of Practice and Procedure.

Section 7482(a)(2) provides in pertinent part:

(a) Jurisdiction.–

(2) Interlocutory orders.–

(A) In general.–When any judge of the Tax Court includes in an interlocutory order a statement that a controlling question of law is involved with respect to which there is a substantial ground for difference of opinion and that an immediate appeal from that order may materially advance the ultimate termination of the litigation, the United States Court of Appeals may, in its discretion, permit an appeal to be taken from such order, if application is made to it within 10 days after the entry of such order.

* * *

In sum, certification of an order pursuant to section 7462(a)(2) is appropriate where the judge verifies that the order: (1) Involves a controlling question of law, (2) with respect to which there is a substantial ground for difference of opinion, and (3) an immediate appeal from that order may materially advance the ultimate termination of the litigation. Failure to meet any one of the three requirements is grounds for denial of certification. See *General Signal Corp. v. Commissioner*, 104 T.C. 248, 251 (1995), citing *Kovens v. Commissioner*, 91 T.C. 74, 77 (1988).

As explained in *Kovens v. Commissioner*, *supra* at 78, the proper application of section 7482(a)(2) requires a balancing of the policies favoring interlocutory appeals, i.e., avoidance of wasted trial and harm to litigants, against the policies underlying the so-called final judgment rule, i.e., avoidance of piecemeal litigation and dilatory and harassing appeals. In *Kovens*, we observed:

> If the avoidance of wasted trial is taken as the sole guide, a multitude of interlocutory opinions will become appealable. This is contrary to the intent of the draftsmen and proponents of 28 U.S.C. sec. 1292(b) (1958) and section 7482(a)(2), who were of the view that interlocutory orders should be granted only in exceptional cases. See 3 U.S. Code Cong. & Admin. News, at 5255, 5259, 5260-5261 (1958). Such a desire to limit availability of this process to exceptional cases reflects a strong policy in favor of avoiding piecemeal review and its attendant delay and waste of time. * * * [Id.]

Petitioners contend that these cases involve a controlling question of law for which there is a substantial ground for difference of opinion and that an immediate appeal may materially advance the ultimate termination of the litigation. We disagree. We are not persuaded that there are substantial grounds for difference of opinion on the points raised in petitioners' motion. Likewise, the issues presented and decided in *Investment Research Associates, Ltd., and Subsidiaries, et al. v. Commissioner*, T.C. Memo. 1999-407, do not justify certification for immediate appeal. Final decisions in those cases have not yet been entered by this Court. In our view an immediate appeal on the issues raised in petitioners' motion would not materially advance the ultimate termination of the litigation in these cases, but rather prolong it, thus defeating the purpose of section 7482(a)(2).

Considering all of the circumstances, and balancing the policies underlying section 7482(a)(2) against the final judgment rule, these cases do not represent the type of exceptional cases warranting an interlocutory appeal. Consequently, we will deny petitioners' request for certification for an interlocutory appeal.

Finally, for reasons previously stated, we will deny petitioners' request that copies of any of the requested materials be made a part of the record in these cases for review by the

Circuit Court of Appeals. See *Estate of Varian v. Commissioner*, *supra*.

Accordingly, after due consideration, it is

ORDERED:

1. That petitioners' Motion for Access to Original Special Trial Judge Report Prepared Under Rule 183(b) is denied in all respects.

2. That petitioners' request to certify this issue for an interlocutory appeal pursuant to section 7482(a)(2), T.R.C., and Rule 193, is denied.

3. That petitioners' request that a copy of the requested materials be made a part of the record in these cases for review by the Circuit Court of Appeals is denied.

/S/ HOWARD A. DAWSON, JR.
HOWARD A. DAWSON, JR.
JUDGE

DATED: WASHINGTON, D.C.
APRIL 26, 2000

UNITED STATES TAX COURT
Washington, D.C. 20217

INVESTMENT RESEARCH ASSOCIATES, LTD., AND SUBSIDIARIES, ET AL.	)	
Petitioners,	)	
v.	)	
	) Docket	
	) Nos.	43966-85, 712-86,
	)	45273-86, 1350-87,
	)	31301-87, 33557-87,
	)	3456-88, 30830-88,
	)	32103-88, 27444-89,
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	)	26251-90, 20211-91,
	)	20219-91, 21555-91,
	)	21616-91, 23178-91,
	)	24002-91, 1984-92,
	)	16164-92, 19314-92,
	)	23143-92, 26918-92,
	)	7557-93, 22884-93,
	)	25976-93, 25981-93.
COMMISSIONER OF INTERNAL REVENUE,	)	
Respondent.	)	

ORDER

For cause, it is

ORDERED: That these cases are reassigned from Special Trial Judge D. Irvin Couvillion to Judge Howard A. Dawson, Jr., for disposition.

After the Special Trial Judge submitted a report, as required by Rule 183(b), Tax Court Rules of Practice and Procedure, these cases were referred to Judge Dawson on September 2, 1998, for review and, if approved, for adoption.

/s/ MARY ANN COHEN
MARY ANN COHEN
CHIEF JUDGE

DATED: WASHINGTON, D.C.
DECEMBER 15, 1999

United States Court of Appeals

For the Seventh Circuit
Chicago, Illinois 60604

October 21, 2003

Before

HON. JOEL M. FLAUM, *Chief Judge*

HON. RICHARD D. CUDAHY, *Circuit Judge*

HON. MICHAEL S. KANNE, *Circuit Judge*

Nos. 01-436, 01-4317, 01-4318, 01-4319,
01-4320, 01-4321, 01-4322 & 02-1220

ESTATE OF BURTON W. KANTER deceased, JOSHUA S. KANTER, executor, and NAOMI KANTER,
Petitioners-Appellants,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent-Appellee.

Appeals from a Decision of the United States Tax Court.

Nos. 712-86, 1350-87, 31301-87, 33557-87, 3456-88, 32103-88, 26251-90

ORDER

On consideration of the petition for rehearing and petition for rehearing *en banc*, no judge in active service has requested a vote on the petition for rehearing *en banc* and a majority of the judges on the original panel have voted to deny rehearing.

It is, therefore, ORDERED that rehearing and rehearing *en banc* are DENIED.

U.S. CONSTITUTION: FIFTH AMENDMENT

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

* * *

26 U.S.C. § 7443A. SPECIAL TRIAL JUDGES

(a) Appointment.–The chief judge may, from time to time, appoint special trial judges who shall proceed under such rules and regulations as may be promulgated by the Tax Court.

(b) Proceedings which may be assigned to special trial judges.–The chief judge may assign–

(1) any declaratory judgment proceeding,

(2) any proceeding under section 7463,

(3) any proceeding where neither the amount of the deficiency placed in dispute (within the meaning of section 7463) nor the amount of any claimed overpayment exceeds $50,000,

(4) any proceeding under section 6320 or 6330, and

(5) any other proceeding which the chief judge may designate,

to be heard by the special trial judges of the court.

(c) Authority to make court decision.–The court may authorize a special trial judge to make the decision of the

court with respect to any proceeding described in paragraph (1), (2), (3), or (4) of subsection (b), subject to such conditions and review as the court may provide.

(d) Salary.--Each special trial judge shall receive salary–

(1) at a rate equal to 90 percent of the rate for judges of the Tax Court, and

(2) in the same installments as such judges.

(e) Expenses for travel and subsistence.–Subsection (d) of section 7443 shall apply to special trial judges subject to such rules and regulations as may be promulgated by the Tax Court.

* * *

26 U.S.C. § 7459. REPORTS AND DECISIONS

(a) Requirement.–A report upon any proceeding instituted before the Tax Court and a decision thereon shall be made as quickly as practicable. The decision shall be made by a judge in accordance with the report of the Tax Court, and such decision so made shall, when entered, be the decision of the Tax Court.

(b) Inclusion of findings of fact or opinions in report.–It shall be the duty of the Tax Court and of each division to include in its report upon any proceeding its findings of fact or opinion or memorandum opinion. The Tax Court shall report in writing all its findings of fact, opinions, and memorandum opinions. Subject to such conditions as the Tax Court may by rule provide, the requirements of this subsection and of section 7460 are met if findings of fact or opinion are stated orally and recorded in the transcript of the proceedings.

* * *

26 U.S.C. § 7461(a), (b). PUBLICITY OF PROCEEDINGS

(a) General rule.–Except as provided in subsection (b), all reports of the Tax Court and all evidence received by the Tax Court and its divisions, including a transcript of the stenographic report of the hearings, shall be public records open to the inspection of the public.

(b) Exceptions.–

(1) Trade secrets or other confidential information.–The Tax Court may make any provision which is necessary to prevent the disclosure of trade secrets or other confidential information, including a provision that any document or information be placed under seal to be opened only as directed by the court.

(2) Evidence, etc.–After the decision of the Tax Court in any proceeding has become final, the Tax Court may, upon motion of the taxpayer or the Secretary, permit the withdrawal by the party entitled thereto of originals of books, documents, and records, and of models, diagrams, and other exhibits, introduced in evidence before the Tax Court or any division; or the Tax Court may, on its own motion, make such other disposition thereof as it deems advisable.

* * *

TAX COURT RULE 183. OTHER CASES

Except in cases subject to the provisions of Rule 182 or as otherwise provided, the following procedure shall be observed in cases tried before a Special Trial Judge:

(a) Trial and Briefs. A Special Trial Judge shall conduct the trial of any such case assigned for such purpose. After such trial, the parties shall submit their briefs in accordance with the provisions of Rule 151. Unless otherwise directed, no further briefs shall be filed.

(b) Special Trial Judge's Report. After all the briefs have been filed by all the parties or the time for doing so has expired, the Special Trial Judge shall submit a report, including findings of fact and opinion, to the Chief Judge, and the Chief Judge will assign the case to a Judge or Division of the Court.

(c) Action on the Report. The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions. Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct.

* * *

FORMER RULE 182. POST-TRIAL PROCEDURE

Except in small tax cases (see Rule 183) or as otherwise provided, the following procedure shall be observed in cases tried before a commissioner:

(a) Proposed Findings and Briefs: Each party shall file his initial brief, including his proposed findings of fact and legal argument, within 60 days after the date on which the trial is concluded, unless otherwise directed. A party thereafter desiring to file a responsive brief shall do so, including any objections to any proposed findings of fact, within 30 days after the expiration of the period for filing the initial brief, unless otherwise directed. With respect to the content, form, number of copies, and other applicable requirements, the proposed findings of fact and the briefs conform to the provisions of Rule 151.

(b) Commissioner's Report: After all the briefs have been filed by all the parties or the time for doing so has expired, the commissioner shall file his report, including his findings of fact and opinion. A copy of the report shall forthwith be served on each party.

(c) Exceptions: Within 45 days after service of the commissioner's report, a party may file with the Court a brief setting forth any exceptions of law or of fact to that report. Within 30 days of service upon him of such brief, any other party may file a brief in response thereto. In any brief filed pursuant to this paragraph, a party may rely in whole or in part upon the briefs previously submitted by him to the commissioner under paragraph (a) of this Rule 182. Unless a party shall have proposed a particular finding of fact, or unless he shall have objected to another party's proposed finding of fact, the Court may refuse to consider his exception to the commissioner's report for failure to make such a finding desired by him or for inclusion of such finding proposed by the other party, as the case may be.

(d) Oral Argument and Decision: The Division to which the case is assigned may, upon motion of any party or on its own motion, direct oral argument. The Division inter alia may adopt the commissioner's report or may modify it or may reject it in whole ~~or in part~~, or may receive further evi-

dence, or may recommit it with instructions. Due regard shall be given to the circumstance that the commissioner had the opportunity to evaluate the credibility of witnesses; and the findings of fact recommended by the commissioner shall be presumed to be correct.

Supreme Court, U.S.
FILED
MAR 2 2 2004
OFFICE OF THE CLERK

(2)

No. 03-1034

In the Supreme Court of the United States

ESTATE OF BURTON W. KANTER, DECEASED, ET AL.,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTIONS PRESENTED

When a case is assigned to a Special Trial Judge of the Tax Court, the Special Trial Judge is to make a "report, including findings of fact and opinion, to the Chief Judge, and the Chief Judge will [then] assign the case to a Judge or Division of the Court." T.C. R. 183(b). The Judge to whom the case is thus assigned "may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part." T.C. R. 183(c). The questions presented in this case are:

1. Whether the Due Process Clause requires that the "original" report of the Special Trial Judge be made public by inclusion in the record.

2. Whether 26 U.S.C. 7459(b), 7461(a), (b), or 7482 requires that the "original" report of a special trial judge be made public by inclusion in the record.

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In the Supreme Court of the United States

No. 03-1034

ESTATE OF BURTON W. KANTER, DECEASED, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-97a) is reported at 337 F.3d 833. The opinion of the Tax Court (Pet. App. 98a) is reported at 78 T.C.M. (CCH) 951. The orders of the Tax Court denying petitioners' post-judgment motions (Pet. App. 99a-103a, 107a-112a) are unreported.

JURISDICTION

The judgment of the court of appeals was entered on July 24, 2003. A petition for rehearing was denied on October 21, 2003 (Pet. App. 115a). The petition for a writ of certiorari was filed on January 20, 2004 (a

Tuesday following a holiday). The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Burton Kanter, a tax attorney, along with Claude Ballard and Robert Lisle, both vice-presidents of Prudential Life Insurance Co. of America, participated in a scheme in which five persons seeking to do business with Prudential paid kickbacks for such business to Kanter. Kanter then divided the money among himself, Ballard, and Lisle by funneling that money through a complex web of corporations, partnerships and trusts. Pet. App. 16a-17a, 23a-68a.

Kanter failed to report the kickbacks he received as income on his federal income tax returns. After discovering the kickbacks, the Commissioner issued notices of deficiency to Kanter, Ballard and Lisle for the resulting income tax deficiencies and, later, asserted civil fraud penalties. Pet. App. 14a.

2. Kanter, Ballard, and Lisle each sought review of the Commissioner's determinations in the Tax Court. Pet. App. 98a. After their cases were consolidated in the Tax Court, the Chief Judge assigned them to be heard by Special Trial Judge D. Irvin Couvillion pursuant to 26 U.S.C. 7443A(b)(4). After a lengthy trial, the special trial judge submitted a report on these consolidated cases to the Chief Judge as required by Tax Court Rule 183(b). The cases were then referred by the Chief Judge to Tax Court Judge Howard A. Dawson for decision. Pet. App. 98a, 113a. On December 15, 1999, the Tax Court issued an opinion in the consolidated cases which states that "[t]he Court agrees with and adopts the opinion of the Special Trial Judge, which is set forth below." *Id.* at 98a. This opinion of the Tax Court sustained the major portion of

the deficiencies and penalties determined by the Commissioner.

3. Kanter, along with Ballard and Lisle, thereafter filed a motion seeking access to "all reports, draft opinions or similar documents prepared and delivered to the Court pursuant to Rule 183(b)." Pet. App. 107a-108a. In the alternative, they asked the Tax Court to make a copy of such materials part of the record in the case. *Id.* at 108a. The Tax Court denied this motion, stating that (*ibid.*):

> In reviewing the Special Trial Judge's report, Judge Dawson gave due regard to the fact that Special Trial Judge Couvillion evaluated the credibility of witnesses, as reflected in the Memorandum Findings of Facts and Opinion (T.C. Memo. 1999-407), and he treated the findings of fact recommended by the Special Trial Judge as being presumptively correct. * * * [T]he provisions of section 7443A(b)(4) and Rule 183 were followed by the Court.

The Tax Court emphasized that "Petitioners appear not to appreciate the distinction between the special trial judges' authority to hear cases and prepare proposed findings and opinions [under 26 U.S.C. 7443A(b)(4)] and their lack of authority actually to decide those cases, which is reserved exclusively for judges of the Tax Court." Pet. App. 109a (quoting *Freytag* v. *Commissioner*, 501 U.S. 868, 874 (1991)). The Tax Court concluded that, "[i]n any event such materials are confidential and not subject to production because they relate to the internal deliberative processes of the Court. Cf. Sec. 7460(b)." *Ibid.*

Kanter then filed a second motion requesting that the special trial judge's report be included in the record

under seal. That motion was also denied by the Tax Court. Pet. App. 101a.

4. Kanter then moved for reconsideration or for a new trial. Pet. App. 99a. Attached to this motion was an affidavit of his counsel, Randall G. Dick. In that affidavit, Dick stated that he had been informed by two or three unnamed judges of the Tax Court that Special Trial Judge Couvillion had recommended in his "original" report that the kickback "payments made by the [persons seeking to do business with Prudential] were not taxable to the individual Petitioners and that the fraud penalty was not applicable." *Id.* at 102a.

The Tax Court denied that motion in an order signed by Chief Judge Thomas B. Wells, Judge Dawson, and Special Trial Judge Couvillion. Pet. App. 103a. The court stated that "[t]he only official Memorandum Findings of Fact and Opinion by the Court in these cases is T.C. Memo. 1999-407, filed on December 15, 1999, by Special Trial Judge Couvillion, reviewed and adopted by Judge Dawson, and reviewed and approved by former Chief Judge Cohen." *Id.* at 102a. The Tax Court stated that the alleged statements purportedly made to Dick were thus "irrelevant and immaterial." *Ibid.* The court further stated that (*ibid.*):

> Judge Dawson states and Special Trial Judge Couvillion agrees, that, after a meticulous and time-consuming review of the complex record in these cases, Judge Dawson adopted the findings of fact and opinion of Special Trial Judge Couvillion, that Judge Dawson presumed the findings of fact recommended by Special Trial Judge Couvillion were correct, and that Judge Dawson gave due regard to the circumstance that Special Trial Judge Couvillion evaluated the credibility of witnesses.

5. Kanter, along with Ballard and Lisle, then filed petitions for mandamus to the Seventh, Eleventh, and Fifth Circuits, respectively, in which they sought orders directing Judge Dawson and the Tax Court to provide them with a copy of the "original" report prepared by Special Trial Judge Couvillion. In the alternative, they sought an order directing the Tax Court to describe any changes made to the initial report submitted by Special Trial Judge Couvillion. The petitions for writs of mandamus were denied. *In re Investment Research Ass'ns & Sub. & Burton W. & Naomi R. Kanter*, No. 00-3369 (7th Cir. Dec. 15, 2000); *In re Ballard*, No. 00-14762-H (11th Cir. Oct. 23, 2000); *In re Lisle*, No. 00-60637 (5th Cir. Sept. 18, 2000).

6. After the entry of final decisions, Kanter's estate, a petitioner herein,[1] appealed to the Seventh Circuit, Ballard appealed to the Eleventh Circuit, and Lisle's executor appealed to the Fifth Circuit. All three of these courts of appeals rejected the assertion that the proceedings in the Tax Court denied the taxpayers due process of law. Pet. App. 1a-97a; *Ballard* v. *Commissioner*, 321 F.3d 1037, 1042-1043 (11th Cir. 2003), petition for cert. pending, No. 03-184; *Estate of Lisle* v. *Commissioner*, 341 F.3d 364, 384 (5th Cir. 2003).

In the present case, the panel majority noted that the Chief Judge of the Tax Court, Judge Dawson, and Special Trial Judge Couvillion all signed the final opinion, and took that statement "at face value." Pet. App. 7a. The court concluded that "Kanter's arguments are immaterial if the Tax Court's final opinion is the [special trial judge's] report." *Ibid.* The court went on to note that, if a quasi-collaborative deliberative pro-

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[1] Kanter died on October 31, 2001, and his estate was substituted as the petitioner in the Tax Court. Pet. App. 1a.

cess between the special trial judge and the Tax Court judge was involved, since the opinion agreed to and adopted by the Tax Court was the ultimate opinion of the special trial judge, any different preliminary recommendation by the special trial judge would no longer be relevant. *Id.* at 13a.

Judge Cudahy concurred in part and dissented in part. Pet. App. 70a-97a. In his view, failure to include a special trial judge's original report in the record violated petitioner's due process right to "meaningful appellate review." *Id.* at 94a.

ARGUMENT

The decision of the court of appeals is correct and does not conflict with any decision of this Court or of any other court of appeals. Further review is therefore not warranted.

Petitioners argue that due process requires that the "original" report of the special trial judge be made public by inclusion in the record so that the appellate court can ensure compliance with Tax Court Rule 183, which provides that the recommended findings of fact of the special trial judge are presumed correct and that due regard be given to the circumstance that the special trial judge had the opportunity to evaluate the credibility of the witnesses. Pet. 13-21. Petitioners similarly argue that Rule 183 requires that findings of the special trial judge contained in his "original" report must be reviewed by the regular Tax Court judge under a clearly erroneous standard, and inclusion of the report in the record on appeal is necessary to determine whether this was done. Pet. 25-29. Finally, petitioners assert that 26 U.S.C. 7459(b), 7461(a) and (b), and 7482 require that the "original" report of a special trial judge be made part of the record on appeal. Pet. 21-25. Peti-

tioners' contentions, which largely reiterate contentions advanced in *Ballard*, petition for cert. pending, No. 03-184, have been rejected by three circuits and are without merit. Pet. App. 1a-97a; *Ballard* v. *Commissioner*, 321 F.3d 1037 (11th Cir. 2003), petition for cert. pending, No. 03-184; *Estate of Lisle* v. *Commissioner*, 341 F.3d 364 (5th Cir. 2003).

1. Petitioners' assertion that they have a due process right to have the "original" report of a special trial judge made public by inclusion in the record fundamentally misperceives the functions and responsibilities of special trial judges and regular judges of the Tax Court in cases assigned to special trial judges for hearing. Authority to determine the facts and law applicable to a case must come from Congress, and Congress has not given the chief judge of the Tax Court authority to allow special trial judges to make the findings and decision in cases that are assigned to them only for hearing. 26 U.S.C. 7443A(b)(4) and (c); see Pet. App. 8a ("The Tax Court thus acts as the original finder of fact."). In light of the requirement that the case must be decided by a regular judge of the Tax Court, Rule 183 provides that reports prepared by special trial judges merely "recommend" findings in the case. T.C. R. 183(c). Thus, the Tax Court, not the special trial judge, was the decisionmaker whose factual findings are subject to appellate review, and petitioners' repeated assertions to the contrary (Pet. 14-19) are simply mistaken.

a. Section 7443A(b)(1)-(3) and (c) of the Internal Revenue Code permit the chief judge of the Tax Court to assign particular types of cases—which are ordinarily small cases—to be heard and decided by special trial judges. 26 U.S.C. 7443A(b)(1)-(3) and (c). At the time relevant to this case, Section 7443A(b)(4) of

the Code (now Subsection (b)(5)) authorized the chief judge to assign "any other proceeding" to special trial judges for hearing and recommended decision only. Any decision in this latter category of cases must be entered by a regular Tax Court judge. 26 U.S.C. 7443A(b)(4) and (c). The present case, involving concealed kickback income received by Kanter, was assigned to the special trial judge only for hearing and recommended decision under this statute. Pet. App. 108a.

The Internal Revenue Code does not prescribe procedures to be employed by the Tax Court in its use of special trial judges. Rather, Congress has authorized the Tax Court to adopt rules prescribing such procedures. 26 U.S.C. 7443A(a), 7453. Rule 183 of the Tax Court was adopted pursuant to this authority. That rule neither authorizes nor requires disclosure to the parties of the reports and recommendations prepared by special trial judges. Instead, in light of the requirement that cases that are assigned only for hearing by a special trial judge must ultimately be decided by a regular judge of the Tax Court (26 U.S.C. 7443A(b)(4) and (c)), Rule 183 states that the reports prepared by the special trial judge merely "recommend" findings and that the judge to whom the chief judge assigns the case "may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions." T.C. R. 183(c).

A judge of the Tax Court to whom a case is ultimately assigned may thus either (i) adopt or abandon the special trial judge's report in its entirety or (ii) modify or otherwise use the special trial judge's report as a step in the fact-finding process. Under Tax Court

Rule 183, as well as under the deliberative processes of courts generally, communications between the judges (and special trial judges) to whom a case is assigned for disposition are not produced or disclosed to the parties. Pet. App. 109a. See *Goetz* v. *Crosson*, 41 F.3d 800, 805 (2d Cir. 1994), cert. denied, 516 U.S. 821 (1995); *United States* v. *Crouch*, 566 F.2d 1311, 1316 (5th Cir. 1978); *In re Cook*, 49 F.3d 263, 265 (7th Cir. 1995); *Fayerweather* v. *Ritch*, 195 U.S. 276, 306-307 (1904). As the court of appeals emphasized in this case, "there is nothing unusual about judges conferring with one another about cases assigned to them." Pet. App. 13a-14a (quoting *Ballard*, 321 F.3d at 1043).

b. It has, moreover, long been settled that, in cases in which due process requires a trial-type hearing, findings may be made by an officer who has "heard" the evidence in the sense of having reviewed and considered the evidence. Due process does not mandate that the officer charged with making the findings and decision also have personally observed the testimony in the case, or that the officer disclose the work product of examiners who observed the evidence, or that particular deference be given to those examiners. See Pet. 19 ("Petitioner does not argue that the Tax Court should * * * be required to hear witnesses."); Pet. App. 84a (Cudahy, J., dissenting) ("[D]ue process does not require that the ultimate fact finder be constrained by a formal degree of deference to the original hearing officer.").

In *Morgan* v. *United States*, 298 U.S. 468 (1936), this Court explained that, while "[t]he one who decides must hear," this does not require personal observation of the witnesses (*id.* at 481-482) (emphasis added):

> Evidence may be taken by an examiner. Evidence thus taken may be sifted and analyzed by competent subordinates. Argument may be oral or written. The requirements are not technical. But there must be a hearing in a substantial sense. And *to give the substance of a hearing*, which is for the purpose of making determinations upon evidence, *the officer who makes the determinations must consider and appraise the evidence which justifies them.*

In *Morgan*, the examiner who personally heard the testimony declined to prepare a tentative report that could then be subject to argument and exceptions before the Secretary to whom the authority to enter the decision had been given by Congress. *Id.* at 475-476. In rejecting the contention that such a procedure was required, this Court stated that, "while it would have been good practice to have the examiner prepare a report and submit it to the Secretary and the parties, and to permit exceptions and arguments addressed to the points thus presented * * * we cannot say that that particular type of procedure was essential to the validity of the hearing." *Id.* at 478.

Similarly, in *Utica Mutual Insurance Co.* v. *Vincent*, 375 F.2d 129, 131 (2d Cir.), cert. denied, 389 U.S. 839 (1967), the court rejected the contention that, "when there are issues of credibility * * * no determination of fact may be made unless the decider has either seen the witnesses himself or has been furnished with a report as to credibility by another." The court stated that "[e]ven on issues where due process requires a 'trial type' hearing, the due process clause makes no such inexorable command." See *NLRB* v. *Mackey Radio & Tel. Co.*, 304 U.S. 333, 350-351 (1938); *Peoria Braumeister Co.* v. *Yellowley*, 123 F.2d 637, 639 (7th

Cir. 1941) ("The right to receive a copy of the findings of the examiner and of his report, with an opportunity to file exceptions and be heard by brief and in oral argument, is a desirable but not essential ingredient of procedural due process and a fair hearing.")[2]

In the analogous circumstance in which a case that has been tried by one judge of the Tax Court is then reviewed by the full Tax Court, Congress has made clear since the very origins of that court that the "original" opinion of the judge who presided at trial is to be excluded from the record. Revenue Act of 1928, ch. 852, § 601, 45 Stat. 871 (26 U.S.C. 7460(b)). And, the courts of appeals have consistently rejected the contention that these procedures contravene due process. *Estate of Varian* v. *Commissioner*, 396 F.2d 753 (9th Cir.), cert. denied, 393 U.S. 962 (1968); *Heim* v. *Commissioner*, 251 F.2d 44 (8th Cir. 1958). See *Towers* v. *Commissioner*, 247 F.2d 233 (2d Cir. 1957), cert. denied, 355 U.S. 914 (1958); *Halle* v. *Commissioner*, 175 F.2d 500, 504 (2d Cir. 1949), cert. denied, 338 U.S. 949 (1950); *Seaside Improvement Co.* v. *Commissioner*, 105 F.2d 990, 992 (2d Cir.), cert. denied, 308 U.S. 618 (1939).

c. Petitioners are similarly mistaken in arguing that due process requires disclosure of a special trial judge's report because the taxpayer has a due process right to ensure that the Tax Court complied with Rule 183(c)'s statement that the recommended findings of fact of the

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[2] Petitioners' reliance (Pet. 17) on *Mazza* v. *Cavicchia*, 105 A.2d 545 (N.J. 1954), is misplaced. *Mazza* rests on state law grounds that are independent of federal law. Moreover, the court in *Mazza* concluded that, since a judge may not consider matters outside of the record in deciding a case, a hearing examiner's report could not be used by a judge unless the report were made part of the record. *Id.* at 554-555. That view erroneously conflates the evidentiary record and deliberations based on that record.

special trial judge are presumed correct and that due regard be given to the circumstance that the special trial judge had the opportunity to evaluate the credibility of the witnesses. Under 26 U.S.C. 7482(a)(1), the courts of appeals review "decisions" of the *Tax Court* "in the same manner and to the same extent" as decisions of the district courts in civil actions tried without a jury. The report of a special trial judge is plainly *not* the "decision" of the Tax Court. 26 U.S.C. 7459; T.C. R. 183(b). Only the decision of the Tax Court, not any "original" recommendation that may have been made by a special trial judge, is the subject of the appellate jurisdiction of the court of appeals.

Moreover, as the court of appeals emphasized in this case, Pet. App. 7a, 13a-14a, petitioners' contention that Rule 183 may have been violated is completely belied by the fact that Chief Judge, Dawson, and Special Trial Judge Couvillion signed orders stating that the decision of the Tax Court was the opinion of the special trial judge. *Id.* at 102a ("Judge Dawson states and Special Trial Judge Couvillion agrees, that * * * Judge Dawson adopted the findings of fact and opinion of Special Trial Judge Couvillion, that judge Dawson presumed the findings of fact recommended by Special Trial Judge Couvillion were correct, and that Judge Dawson gave due regard to the circumstances that Special Trial Judge Couvillion evaluated the credibility of witnesses."); accord *id.* at 108a. Even petitioners concede that the statement that the opinion of the special trial judge was adopted evidences that the opinion issued by the Tax Court states "the final views of the [special] trial judge." Pet. 9. Thus, even assuming that the special trial judge had a view of Kanter's case at the time the judge submitted his "original" report that differed from the views that are reflected in

the opinion ultimately entered in the case, it does not follow that the opinion adopted by the Tax Court was not, in fact, the opinion of the special trial judge.

Petitioners assert that the Tax Court routinely makes changes to the "original" reports prepared by special trial judges without telling the parties. Pet. 4-7. Petitioners claim (Pet. 6) that this is evidenced by the absence of any case decided since Rule 183's adoption in 1984 in which the Tax Court disagreed with a recommended finding by a special trial judge. During the period from 1976 through 1984, however, when parties were provided copies of reports of special trial judges and afforded an opportunity to file exceptions thereto, there were only six cases (out of approximately 680 decisions) in which the Tax Court did not adopt the opinion of the special trial judge. In only one of those opinions, moreover, did the reviewing judge of the Tax Court disagree with or "reverse" the special trial judge. See *Kansas City S. Ry.* v. *Commissioner*, 76 T.C. 1067 (1981); *Narver* v. *Commissioner*, 75 T.C. 53 (1980); *Hilton* v. *Commissioner*, 74 T.C. 305 (1980); *La Fargue* v. *Commissioner*, 73 T.C. 40 (1979); *Orzechowski* v. *Commissioner*, 69 T.C. 750 (1978); *C. Blake McDowell, Inc.* v. *Commissioner*, 67 T.C. 1043 (1977), vacated and remanded, 576 F.2d 718 (6th Cir.), on remand, 71 T.C. 71 (1978), aff'd, 652 F.2d 606 (6th Cir. 1980).[3] There is thus no factual basis for petitioners' assertion that when (as in the present case) the Tax Court issues an

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[3] In several other cases (14 out of approximately 680 cases involving special trial judges that were decided between 1976 and 1984), the Tax Court adopted the opinion of the special trial judge with modifications that were, in most instances, described as "minor." See *Ocean Sands Holding Corp.* v. *Commissioner*, 41 T.C.M (CCH) 1, 2 (1980).

opinion that adopts the report of a special trial judge, it fails accurately to set forth the view of the special trial judge in the case.

At bottom, petitioners challenge the authority of the Tax Court, without public disclosure, to communicate or collaborate with a special trial judge about a case after the judge submits an "original" report to the Chief Judge under Rule 183(b). Yet nothing in Rule 183 forbids such communications, nor does Rule 183 prevent the special trial judge himself from modifying his recommended findings based upon that collaborative process. Nor would such non-public communications or collaborations violate due process. Internal communications among judges and special trial judges are part of the internal deliberative process of the court. Pet. App. 109a. As explained by the court of appeals, "there is nothing unusual about judges conferring with one another about cases assigned to them," and, as a result of such conferences, judges sometimes change their original position or thoughts. *Id.* at 13a-14a (quoting *Ballard*, 321 F.3d at 1043). See *Checkosky* v. *SEC*, 23 F.3d 452, 489-490 (D.C. Cir. 1994) ("[i]n agencies as in courts, votes are not final until decisions are final; and decisions do not become final until they are released, accompanied by an explanation of the reasons for the result"; "the exchange of draft opinions can and does change votes").

Moreover, as discussed above, the record demonstrates that the opinion of the court *does* accurately set forth the opinion reached by Special Trial Judge Couvillion. Pet. App. 98a, 103a. As the court of appeals noted, where (as here) an opinion entered accurately states the views of the special trial judge, any differing preliminary recommendation would no longer have any relevance, because it would not constitute a valid

statement of the special trial judge's view of the case. *Id.* at 13a; accord *Ballard*, 321 F.3d at 1042-1043; *Estate of Lisle*, 341 F.3d at 384.

d. Contrary to petitioners' contention, the court of appeals correctly concluded that Rule 183 does not require regular judges of the Tax Court to review the recommended findings of a special trial judge under a "clearly erroneous" or other deferential standard of review. Pet. App. 8a-9a; see *id.* at 75a (Cudahy, J., concurring in part and dissenting in part) ("I agree with the majority's determination that Rule 183 imposes no requirement of disclosure or of clearly erroneous deference upon the Tax Court."). Rule 183 simply does not embody a "standard of review" in the traditional sense. As discussed, the findings that are reviewed on an appeal from a decision of the Tax Court are the factual findings of the regular judge of the Tax Court. 26 U.S.C. 7443A(c); see, *e.g.*, *Heim*, 251 F.2d at 45-46; *Estate of Varian*, 396 F.2d at 755; *Towers*, 247 F.2d at 237; *Erhard* v. *Commissioner*, 46 F.3d 1470, 1476 (9th Cir.), cert. denied, 516 U.S. 930 (1995). See also, *Morgan*, *supra*; 26 U.S.C. 7460(b).

Because responsibility and authority for the findings and decision is vested in the regular judge assigned to the case and with the Tax Court itself (26 U.S.C. 7443A(c)), Rule 183 does not (and indeed, it could not) permit a regular judge to subordinate his or her judgment as to the findings or decision to that of a special trial judge. See Pet. App. 8a (Rule 183 merely instructs the regular judge "to be cognizant that the [special trial judge] had the opportunity to evaluate the credibility of witnesses"); see also, *e.g.*, *Colorado* v. *New Mexico*, 467 U.S. 310, 317 (1984) (in reviewing exceptions to findings of a special master, the special master's findings "deserve respect and a tacit presumption of correctness"

but "the ultimate responsibility for deciding what are correct findings of fact remains with us"); *Renegotiation Bd.* v. *Grumman Aircraft Eng'g Corp.*, 421 U.S. 168, 185 n.22 (1975) (review limited by "a clearly erroneous or some other deferential standard" would grant "de facto decisional authority").

Petitioners argue (Pet. 25-29) that the court of appeals' reading of Rule 183 conflicts with *Stone* v. *Commissioner*, 865 F.2d 342, 344-347 (D.C. Cir. 1989), rev'g *Rosenbaum* v. *Commissioner*, 45 T.C.M. (CCH) 825 (1983), which held that former Rule 182(d) required that the Tax Court review the recommended findings of the special trial judge for clear error. Petitioner is mistaken. As Judge Cudahy pointed out (Pet. App. 76a-79a), *Stone* was decided under the prior rules of the Tax Court, under which litigants were furnished with copies of special trial judges' recommended findings and conclusions and then were given an opportunity to take exception thereto, with only the exceptions being reviewed by a regular judge of the Tax Court. T.C. R. 182(b) and (c), 60 T.C. 1149 (1973); see *Freytag* v. *Commissioner*, 904 F.2d 1011, 1015 n.8 (5th Cir. 1990), aff'd, 501 U.S. 868 (1991). When the Tax Court adopted Rule 183 in 1983 (effective January 16, 1984), it withdrew the provisions requiring litigants to be furnished with copies of reports of special trial judges and to file exceptions thereto. See notes to Rule 183, reproduced at 81 T.C. 1045, 1070 (1983) ("The prior provisions for service of the Special Trial Judge's report on each party and for the filing of exceptions to that report have been deleted.").

By eliminating the procedures for disclosure and the filing of exceptions, the Tax Court Rules now make it clear that review by a regular judge of a special trial judge's report is not in the nature of an appellate

review but is an exercise of the regular trial judge's original fact-finding authority. T.C. R. 183; see Pet. App. 76a-77a (Cudahy, J., concurring in part and dissenting in part). And although the D.C. Circuit has cited *Stone* since Rule 183 was amended, see *Landry* v. *FDIC*, 204 F.3d 1125, 1133, cert. denied, 531 U.S. 924 (2000), that decision neither involved the correct interpretation of the current Tax Court Rule nor considered whether Rule 183 requires deference under a clearly erroneous standard of review notwithstanding the Tax Court's determination to withdraw procedures for service and exceptions to a special trial judge's report. Finally, as discussed, because the Tax Court decision in this case in fact adopts in whole "the findings of fact and opinion of Special Trial Judge Couvillion," Pet. App. 102a, the issue of whether Rule 183 requires particular deference to the recommended findings of the special trial judge is entirely moot. *Id.* at 7a.

e. Petitioners' also assert that they are entitled to the special trial judge's so-called original report by virtue of "long-established judicial practice." Pet. 16. Unlike litigation that must be assigned to an Article III court for adjudication, however, tax cases are "public rights" cases, which "Congress may or may not bring within the cognizance of the courts of the United States, as it may deem proper." *Crowell* v. *Benson*, 285 U.S. 22, 50 (1932) (quoting *Murray's Lessee* v. *Hoboken Land & Improvement Co.*, 59 U.S. (18 How.) 272, 284 (1855)); see *North Pipeline Constr. Co.* v. *Marathon Pipe Line Co.*, 458 U.S. 50, 68, 70 n.22 (1982); *Ex parte Bakelite Corp.*, 279 U.S. 438, 451 (1929). See *Morgan*, *supra*.[4] During the first two years after creation of the

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[4] Although petitioners note that this case involved a civil fraud penalty (Pet. 8), public rights cases include tax cases in which the

Board of Tax Appeals (the predecessor to the Tax Court), decisions of the Board were not appealable. Instead, a litigant dissatisfied with the decision in the case had to bring a separate action in an appropriate court to challenge the Board's decision. Congress subsequently created a statutory right of direct review of decisions of the Board of Tax Appeals. *Old Colony Trust Co.* v. *Commissioner*, 279 U.S. 716, 721 (1929).

Nor were tax cases subject to procedures at common law similar to those of present day Article III courts. At common law, tax cases were resolved in a branch of the "court of exchequer" and were not "judicial controversies * * * according to the ordinary course of the common law or equity." *Murray's Lessee*, 59 U.S. (18 How.) at 282. The Exchequer was a "department" in which "a court [of revenue] [was] held before the Treasurer," and which was "probably the nearest approach to a body of administrative law that the English legal system has ever known; and the court of Exchequer, sitting as a court of Revenue, is the nearest approach to an administrative court."[5] 9 W. Holdsworth, *A History of English Law* 231, 239 (1926). See

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Government asserts penalties. See *Atlas Roofing Co.* v. *Occupational Safety & Health Review Comm'n*, 430 U.S. 442, 450 (1977) (emphasis added) ("public rights" doctrine extends to cases that involve "taxes * * * *together with penalties*"); *Helvering* v. *Mitchell*, 303 U.S. 391, 401 (1938) (noting that the civil fraud penalty is "provided primarily as a safeguard for the protection of the revenue and to reimburse the Government for the heavy expense of investigation and the loss resulting from the taxpayer's fraud").

[5] Petitioners' reliance (Pet. 15-16) on *Mathews* v. *Eldridge*, 424 U.S. 319 (1976), is misplaced. *Mathews* involved a party's right to a hearing before being deprived of property. Kanter received a full pre-deprivation hearing. *Mathews* requires no more—and often much less.

A. Carter, *A History of the English Courts* 51 (7th ed. 1944). Accordingly, due process does not prohibit the use of procedures in federal tax cases similar to those sustained in *Morgan* or mandated by Congress in 26 U.S.C. 7460(b), and does not require that the Tax Court operate in a manner identical to Article III courts. Indeed, taxpayers who wish to avail themselves of an Article III forum can do so by paying the asserted deficiency and suing for a refund in accordance with the procedures set forth in 26 U.S.C. 7422, 6511, 6532.

2. There is also no merit to petitioners' assertion (Pet. 21) that 26 U.S.C. 7461(a) and 7459(b) require that "original" reports of special trial judges be included in the record. Petitioners raised no issue under Section 7461(a) in his briefs below, and referred to Section 7459(b) for the first time in their reply brief. The contentions thus were waived in the court of appeals (*United States* v. *Magana*, 118 F.3d 1173, 1198 n.15 (7th Cir. 1997), cert. denied, 522 U.S. 1139 (1998)), and are therefore not properly before this Court. *TRW Inc.* v. *Andrews*, 534 U.S. 19, 34 (2001); *Holly Farms Corp.* v. *NLRB*, 517 U.S. 392, 400 n.7 (1996); *Lawn* v. *United States*, 355 U.S. 339, 362 n.16 (1958).

In any event, 26 U.S.C. 7461(a) does not require disclosure of documents prepared by a special trial judge but states that "reports of the Tax Court" and "evidence" received by the court are public records that are open to inspection by the public. See H.R. Conf. Rep. No. 844, 68th Cong., 1st Sess. 30 (1924) ("the Board shall make a report * * * of its findings of fact and its opinion and decision in each case * * * [and] such report and all evidence received by the Board shall be public records"). A report that a special trial judge prepares for submission to the chief judge and is assigned to a regular judge is described in Rule 183(c)

as "the Special Trial Judge's report." It is neither a report "of the Tax Court" nor "evidence."

Similarly, 26 U.S.C. 7459(b) does not require disclosure of a special trial judge's "original" report. Section 7459(b) states that the Tax Court shall report all of "*its* findings of fact, opinions, and memorandum opinions" (emphasis added). As discussed, recommendations in reports of special trial judges are not findings or opinions of the Tax Court.

Petitioners' reliance on 26 U.S.C. 7482 is equally unavailing. That statute provides that courts of appeals are to review "decisions" of the Tax Court "in the same manner and to the same extent" as decisions of the district courts in civil actions tried without a jury. The report of a special trial judge, however, is plainly *not* the "decision" of the Tax Court. As noted above, it is the decision of the Tax Court, not the recommendation of the special trial judge (either initial or final), that is the subject of the appellate jurisdiction of the courts of appeals. Pet. App. 9a.

3. The courts of appeals that have addressed the precise questions presented in this case are fully in accord with the decision of the court of appeals below. In *Ballard*, the Eleventh Circuit rejected the contention that the procedures employed by the Tax Court violated the taxpayer's due process rights. In *Estate of Lisle*, the Fifth Circuit agreed with the decision below and the decision of the Eleventh Circuit in *Ballard*. 341 F.3d at 384. See *Erhard*, 46 F.3d at 1475-1476 (upholding review by a regular judge of special trial judge's recommendation under the procedures in Rule 183(c) in which litigants are not provided a copy of the special trial judge's recommendations). There is thus no conflict or other reason to warrant granting a writ of certiorari in this case.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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No. 03-1034

In the Supreme Court of the United States

ESTATE OF BURTON W. KANTER, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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1. The Issues Are Of Exceptional National Importance. The government attempts to portray this case as a run-of-the-mill dispute despite the fact that it involves a circuit split and a remarkable practice of judicial secrecy that raises serious due process and statutory issues. The Tax Court practice at issue has created a furor in the Tax Court bar and generated national legal concern. The government considers it irrelevant (Opp. at 6, 14) that the Tax Court affirmatively misleads the Courts of Appeals and taxpayers by manipulating the record to hide conflicts between the recommended factual findings of its trial judges (STJs) and the ultimate findings of the Tax Court. The Courts of Appeals routinely review "credibility" and "intent" findings in Tax Court decisions without knowing whether those published findings conceal – as the government does not dispute is true here – a complete contradiction between the trial judge and the Tax Court judge who, having heard none of the witnesses, nonetheless overturns the trial judge's findings and credibility judgments.

Neither the Tax Court's rules nor anything the government points to publicly explains that the Tax Court asserts the power to secretly overturn its trial judges' recommended findings without the record reflecting that reality. The Courts of Appeals, legally required to determine whether Tax Court findings are "clearly erroneous," are denied knowledge of when the Tax Court's published findings conflict with those filed by the trial judge. The appellate courts have no basis for comparing the findings, inferences, and conclusions in the trial judge's report and the Tax Court's ultimate decision. The straightforward legal question presented – which the government's brief obscures – is whether non-disclosure of the trial judge's report violates due process, Congress's repeated mandate that all Tax Court reports and findings be public, or the statutory right to appellate review based on the full record.

2. There Are No Facts In Dispute. The government does not dispute that the issue of secret STJ reports is a recurring one in a large category of important tax cases every year. It does not deny Kanter's showing that STJs are used in 50-89 cases a year involving the process at issue here, or that the Tax Court keeps secret the STJ reports in every one of these cases. The government does not disagree that these secret STJ reports affect massive amounts in tax liabilities, including the more than $30 million at issue here and the $1.5 billion at issue in *Freytag v. Commissioner*, 501 U.S. 868, 871 n.1 (1991). Nor does the government deny that these STJ reports were, for many years, routinely made available.

With respect to this case, the government does not dispute what three judges of the Tax Court have reported: that the experienced STJ who alone heard all the witnesses, actively questioned most of them, and then filed a detailed, lengthy opinion – after more than four years of reviewing the case – found that the taxpayers had testified credibly; that they were not personally liable for the monies at issue in this appeal *at all*, let alone for fraud; and that all of the income was properly reported for tax purposes by the entities to which it was paid.

The government also does not deny what these three judges of the Tax Court further reported: that the Tax Court judge, who heard none of the witnesses, re-wrote the STJ's opinion, made an "outright rejection"[1] of the STJ's credibility findings, and completely changed the STJ's "findings relating to credibility and fraud."[2] Thus, the government does not deny that, in this multi-million-dollar dispute, a head-on contradiction exists between the trial

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[1] *Declaration of Attorney Randall G. Dick* ¶ 7, Seventh Cir. App. 250-252; see also Pet. App. 73a n.1 (*Declaration* cited in Judge Cudahy's dissent).

[2] *Id.* at ¶ 5.

judge's recommended findings and the Tax Court's ultimate findings. Nor does the government deny that the Courts of Appeals were asked to review this decision without access to the basis for these diametrically opposed conclusions.

3. Secret Trial Judge Reports Violate Due Process. The government offers three reasons that secret STJ reports purportedly do not violate due process or federal statutes. First, the government dismisses the STJ's report as of no "relevance" because it does not embody the final "decision" of the Tax Court. Opp. at 12, 14. This is a remarkable assertion. Even though the report is not the final disposition of the case, the Tax Court's own rules require the STJ to file this report; those rules further require that the Tax Court "shall" give "[d]ue regard" to the fact that the STJ "had the opportunity to evaluate the credibility of witnesses" and "shall" presume correct the STJ's findings of fact. Tax Ct. R. 183(b), (c). These are legal mandates to which the Tax Court is obligated to adhere. See, *e.g.*, *Service v. Dulles*, 354 U.S. 363, 388 (1957). The Courts of Appeals are in direct conflict on exactly how strong Rule 183's constraint is on the Tax Court's power to reverse its trial judges, but there is no dispute that Rule 183 gives the STJ's report direct legal significance, whatever the exact quantum of deference required. Further, as Judge Cudahy explained below, to engage in proper appellate review, the courts must know whether a credibility "finding" comes from the trial judge.

The STJ's reports are initial *judicial* findings of fact, like those of federal magistrate judges and court-appointed special masters. The STJs are *judges*. Their reports are not law clerk memoranda or similar internal communications within a judge's chambers. Internal communications do not enjoy a legal presumption of correctness, as do the STJ's findings; law clerks and similar employees are not charged with the responsibility to hear witnesses, rule on admissibility of evidence, make credibility determinations, or submit detailed formal opinions. The government's

argument that the trial judge might have changed his mind by the time of the Tax Court's ultimate decision is beside the point, for it is the Rule 183 report, which must be filed, to which the Tax Court is required to give deference.

The government does not disagree with Kanter's showing that no other court or even administrative agency in the federal system is permitted to conceal such initial findings and credibility judgments. Indeed, as Judge Cudahy wrote in dissent, "I can think of no single item of *more* significance in evaluating a Tax Court's decision on fraud than the unfiltered findings of the STJ who stood watch over the trial." Pet. App. 93a (emphasis added). The government does not explain how appellate courts can perform proper appellate review, especially where intent and credibility are critical, absent complete information regarding fundamental conflicts – like that between no tax liability and fraud – between trial judge and Tax Court findings.

Second, the government repeatedly argues that Kanter "misperceives" the allocation of responsibility between STJs and Tax Court judges. Opp. at 7. But Kanter's petition consistently recognizes that STJs make initial or recommended findings. Kanter does not argue that the STJ's may decide cases, but only that their legally-mandated findings must be included in the record. There is nothing novel in this. What is novel is that the Tax Court, unlike any other federal judicial or administrative body, refuses to release the initial STJ findings so that the Courts of Appeals can engage in proper appellate review.

The government's lecture about divisions of responsibility under 26 U.S.C. § 7443A(b)(4) and (c) thus obscures the essential legal point: STJ reports must be part of the record on review. The findings of administrative law judges and other initial hearing officers must be part of the record under the Administrative Procedure Act, even when an agency has de novo fact-finding power. 5 U.S.C. § 557(c)

("All decisions, including initial, recommended, and tentative decisions, are a part of the record * * *."). Kanter's simple claim is that due process and federal statutes require at least the same of the Article I Tax Court – particularly because the Tax Court is required to presume the STJ's findings to be correct.

Third, the government exaggerates the narrow claim Kanter is making. Kanter does not "challenge the authority of the Tax Court, without public disclosure, to communicate or collaborate with a special trial judge about a case after the judge submits an 'original' report to the Chief Judge under Rule 183(b)." Opp. at 14. Kanter argues only that, whatever communications take place, the record must include the Rule 183 Report with its recommended findings.

4. The Circuits Are In Conflict. The government attempts to avoid the direct conflict that exists. The D.C. Circuit holds that the Tax Court's own rules permit it to overturn STJ findings only when "clearly erroneous." *Stone v. Comm'r*, 865 F.2d 342, 344 (D.C. Cir. 1989). In stark contrast, the decision below held that these rules do not require "any particular level of deference" at all to the STJ's findings. This conflict over the reviewing power of the Tax Court was reserved in *Freytag*. 501 U.S. at 874 n.3. Its resolution is critical to the proper structure of Tax Court adjudication. Both the D.C. Circuit and the Seventh Circuit interpreted the identical language in the relevant Tax Court rules: "Due regard shall be given to the circumstance that the commissioner [since re-named the special trial judge] had the opportunity to evaluate the credibility of witnesses; and the findings of fact recommended by the commissioner shall be presumed to be correct." Tax. Ct. R. 182(d), 60 T.C. 1150 (1973), renumbered as current Tax Ct. R. 183(c). But the circuits reached directly conflicting results concerning the legal effect of this language.

The government attempts to distinguish the cases on the ground that the current Rule dropped the earlier requirement that the commissioner's (or STJ's) report be served on the parties. But that procedural modification regarding the report's *disclosure* cannot possibly affect the plain meaning of the unaltered legal text concerning the standard of review. The plain language of Rule 183 continues, in identical terms, to require the Tax Court to adhere to the "presumed correct" and "due regard" standards. Withholding the STJ's report no more changes the review role of the Tax Court than non-publication of District Court opinions would change the review role of the Courts of Appeals. The government cannot point to any history that suggests the Tax Court *intended* to change its review role, but even such evidence would not be enough to alter the meaning of the Rule's unchanged text. See *Bedroc Ltd., LLC v. United States*, 541 U.S. __ (2004) (slip op. at 6-7). Moreover, the Seventh Circuit viewed its "no deference at all" holding as compelled by the statutory structure of the Tax Court (Pet. App. 8a) – a view in direct conflict with the D.C. Circuit's interpretation of the statutes. This conflict on the review role the statutes permit or require the Tax Court to play does not turn on whether the Tax Court's internal rule has been modified to deny access to the STJ report.

There also is no doubt that *Stone* continues to govern in the D.C. Circuit. Judge Williams in *Stone* noted that the Tax Court had used language with a "well-established meaning" and that "until the [tax] court adopts new language, it must hew to the meaning of what it has said." *Stone*, 865 F.2d at 347. The Tax Court has not adopted any such new language. The D.C. Circuit has never questioned *Stone*, and as the government concedes (Opp. at 17) has recently endorsed *Stone*. *Landry v. FDIC*, 204 F.3d 1125, 1133 (D.C. Cir. 2000) (distinguishing FDIC's de novo fact-finding powers from limitation of Tax Court to "clearly erroneous" review of its STJs). Indeed, *Landry* expressly cited current Rule 183(c)

(*id.*), which makes clear that the D.C. Circuit continues to adhere to *Stone*. The government suggests the conflict is "moot" because the Tax Court said it adopted "the opinion" of the STJ. Opp. at 17. But the government does *not* argue (because it would not be true) that the Tax Court adopted the original STJ report. *That* is the report to which Rule 183 requires deference, whether under the "clearly erroneous" standard or some lesser one, and the conflict over the Rule's meaning remains live.

5. The Tax Court Violates Congress's Commands. Congress has legislated numerous times, for at least 80 years, to attempt to ensure full transparency, accountability, and fairness in tax proceedings. Yet unlike other judicial bodies, the Tax Court regularly refuses to disclose legal decisions and actions it takes. That is true concerning not only the practice at issue, but other Tax Court practices as well. See, *e.g.*, Leandra Lederman, *Tax Court S Cases: Does the "S" Stand for Secret?*, 79 TAX NOTES 257 (April 13, 1998) (criticizing as illegal the Tax Court's denial of public access to decisions in small-tax cases). Congressional statutes variously provide that "all reports," "all evidence," and all "findings of fact, opinions, and memorandum opinions" in tax proceedings must be disclosed. 26 U.S.C. §§ 7461(a), 7459(b). These broadly-worded statutes were specifically enacted to regularize tax court proceedings and rid them of secretive processes. The Tax Court's own rules numerous times deem the product of the STJs to be "reports" that must contain "findings of fact." Tax Ct. R. 183(b), (c). The statutory disclosure mandates for "all reports" and "findings of fact" thus apply to the STJ's reports. At the very least, these statutes should be construed to require disclosure to avoid the substantial constitutional issues otherwise presented. Certiorari is warranted to address the Tax Court's repeated attempts to operate outside the system of transparency that Congress has required and under which all other federal judicial and administrative bodies operate.

This issue was raised below and the lower court expressly passed on it; indeed, Judge Cudahy dissented on this issue. Pet. App. 7a, 9a, 11a, 80-83a, 96a. The issue is therefore properly presented. See *United States v. Williams*, 504 U.S. 36, 40-41 (1992). See also Appellant's Petition for Rehearing and for Rehearing En Banc, at 13; Appellant's Reply Brief, at 9 n.3.

These statutes, and the relevant due process principles that animate them, should also be construed to reflect the common-law right and legal presumption that favors public disclosure of all judicial records and documents on which the decision-making tribunal is legally required to rely. See, *e.g.*, *Nixon v. Warner Communications, Inc.*, 435 U.S. 589, 597 (1978). The government rejects this principle on the theory that the Tax Court was once an executive agency, like the ancient English "court of exchequer." But in another important effort to ensure regularity and fair administration of the tax system, Congress in 1969 established the United States Tax Court as an Article I "court of record." 26 U.S.C. § 7441. Congress granted the Tax Court additional judicial powers, such as the power to punish contempt, and conclusively established that the Tax Court would "no longer be an independent agency in the executive branch." HAROLD DUBROFF, THE UNITED STATES TAX COURT: AN HISTORICAL ANALYSIS 213 (1979).

The Tax Court is now a judicial institution of the United States. See *Freytag*, 501 U.S. at 891. Legal presumptions about fair and proper judicial administration, such as public accessibility to decisional documents, apply to it as to other federal judicial institutions. See also Brief *Amicus Curiae* of Sen. David Pryor *et al.* in Support of Petition for Certiorari in *Ballard v. Commisioner*, No. 03-184, at 8-10 (discussing Omnibus Taxpayer Bill of Rights, 102 Stat. 3342, 3731). Indeed, the government cannot have it both ways. If instead the Tax Court were somehow deemed an executive agency, it would have to comply with the APA. But the APA leaves no

doubt that the reports of hearing officers like STJs must be included in the record on review. See *supra* at 4-5.

The appellate review statute (26 U.S.C. § 7482(a)(1)) also requires the Courts of Appeals to review "decisions" of the Tax Court "in the same manner and to the same extent" as decisions of the district courts in non-jury civil actions. The government argues this statute does not require disclosure of the STJ report because appellate review is only of the "decision" of the Tax Court itself. Kanter, of course, fully recognizes that the STJ's report is not itself the final decision of the Tax Court. Kanter's argument is that proper appellate review *of the Tax Court's decision* requires that the record include the presumptively-correct STJ report. The government does not explain how the Courts of Appeals can conduct the statutorily-required review if the record does not reflect that, as in this case, the Tax Court has overturned the findings and credibility judgments of the trial judge. Just as the reports of magistrates, bankruptcy judges, and special masters are part of the record on review of decisions of district courts (see Pet. at 16-17), the reports of STJs must be part of the record to ensure proper appellate review.

6. The STJ Found Petitioner Not Liable. The government's tendentious use of the term "kickbacks" reveals precisely why due process must enable the appellate courts to review the complete record. Although the government seeks to poison the Court's exercise of its discretion by suggesting that Kanter concealed some kind of illegal income, all income from the transactions at issue was fully reported for tax purposes by the entities to which it was paid. The dispute is whether the income should have been reported by Kanter personally, as the government claimed, or by the entities that actually received the monies, as Kanter, one of the leading tax lawyers and writers in the country, claimed. An experienced judge, sitting since 1985, found that Kanter had properly paid all taxes, testified credibly, and was not liable for taxes, let alone for fraud. Even without the

STJ's report, the Fifth Circuit has already overturned, as clearly erroneous, the Tax Court's finding of fraud with respect to one of the other taxpayers involved. *Estate of Lisle v. Comm'r*, 341 F.3d 364 (5th Cir. 2003).

7. Numerous Commentators Have Concluded That Secret STJ Reports Violate Due Process And Federal Law. Since this litigation revealed that the Tax Court asserts the power to reverse its trial judges findings without the record reflecting that fact, there has been an outpouring of commentary in the professional journals. Virtually all this commentary strongly criticizes the Tax Court and argues that its secret practices violate due process and federal law. See, *e.g.*, Eric Winwood, *The Reclusive Report: The Tax Court Denies Due Process By Not Disclosing Special Trial Judge Reports To Litigants*, 2004 FED. CTS. L. REV. 3; Leandra Lederman, *Transparency and Obfuscation in Tax Court Procedure*, 102 TAX NOTES 1539, 1541 (March 22, 2004) (non-disclosure of the STJ report improperly "shields the [tax] court from accountability"); Gerald A. Kafka & Jonathan Z. Ackerman, *Fact-Finding in the Tax Court: Access to Special Trial Judge Reports*, 91 TAX NOTES 639, 642 (April 23, 2001) ("There seems to be little justification for the Tax Court to shroud its judicial processes from the public and the parties to a greater extent than any other federal court."); Cornish F. Hitchcock, *Public Access to Special Trial Judge Reports*, 2001 TAX NOTES TODAY 199-41 (Oct. 12, 2001) (non-disclosure of STJ report violates common-law and constitutional rights of access to judicial documents). See also Marcia Coyle, *Secrecy in Tax Court Proceeding Challenged*, NATIONAL LAW JOURNAL, March 15, 2004, at 1 (noting national significance of issue). This extensive, critical commentary confirms that this case poses important issues of national concern that warrant the grant of certiorari.

Respectfully submitted.

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APRIL 2004

(9) (7)

Nos. 03-184 and 03-1034

Supreme Court, U.S.
FILED
AUG 2 - 2004
OFFICE OF THE CLERK

IN THE

Supreme Court of the United States

CLAUDE M. BALLARD AND MARY B. BALLARD,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

ESTATE OF BURTON W. KANTER, ET AL.,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Seventh and Eleventh Circuits

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IN THE UNITED STATE COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

01-172949-GG

CLAUDE M. BALLARD,

v.

C.I.R.

DOCKET ENTRIES

File Date	Entry	Party
01/24/2002	Motion to Stay Proceedings: Appellant-Ballard, Claude M. (Atty: Steven Spencer Brown)	Claude M. Ballard
01/31/2002	Response in Opposition to Motion to Stay Appeals	
02/01/2002	Reply in Support of Motion to Stay	
03/27/2002	Appellant's Brief Filed: Appellant-Ballard, Claude M. (Atty: Robert Edwin Davis): Appellant-Ballard, Mary B. (Atty: Robert Edwin Davis)	Mary B. Ballard
05/06/2002	Appellee Brief Filed: Appellee-Commissioner of Internal Revenue, (Atty: Joan I. Openheimer)	
05/30/2002	Reply Brief Filed: Appellant-Ballard, Claude M. (Atty: Robert Edwin Davis): Appellant-Ballard, Claude M. (Atty: Robert Edwin Davis): Appellant-Ballard, Mary B. (Atty: Robert Edwin Davis)	

07/29/2002	Appellant's Unopposed Motion for additional time for oral argument is hereby GRANTED..in part. Each side shall have (20) Twenty minutes for oral argument..: (Atty: Vester T. Hughes, Jr.)	
02/13/2003	OPINIA (Opinion - Issuance with Costs) issued. costs taxed against petitioners-appellants. cc: Brown, Steven Spencer cc: Hughes, Vester T., Jr. cc: Davis, Robert Edwin cc: Schenck, David J. cc: Martin, Royal B., Jr. cc: Openheimer, Joan I. cc: Gibson, J+	
02/13/2003	Judgment Entered	
03/28/2003	Petition for Rehearing En Banc: Ballard, Claude M., Ballard, Mary B. (Atty: Robert Edwin Davis):	Claude M. Ballard
05/22/2003	The motion of Appellants, for STAY of the issuance of the mandate pending petition for writ of certiorari is GRANTED to and including 8/4/03...PTF/See file for Complete Text	

IN THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

ESTATE OF BURTON W. KANTER,
Plaintiff/Petitioner,
v.

C.I.R.,
Defendant.

DOCKET ENTRIES

DATE	ENTRY
12/26/01	Tax court case docketed. [01-4316] [1465040-1] Appellant's brief due 2/5/02 for Estate Burton Kanter. Docketing Statement due 1/3/02. (land) [01-4316]
9/4/02	Case heard and taken under advisement by panel: Chief Judge Joel M. Flaum, Circuit Judge Richard D. Cudahy, Circuit Judge Michael S. Kanne. [01-4316, 01-4317, 01-4318, 01-4319, 01-4320, 01-4321, 01-4322, 02-1220] [1544207-1] (broo) [01-4316 01-4317 01-4318 01-4319 01-4320 01-4321 01-4322 02-1220]
7/24/03	Filed opinion of the court PER CURIAM. We AFFIRM in part and REVERSE in part the decision of the Tax Court. Chief Judge Joel M. Flaum, Circuit Judge Richard D. Cudahy, concurring in part and dissenting in part, Circuit Judge Michael S. Kanne. [01-4316, 01-4317, 01-4318, 01-4319, 01-4320, 01-4321, 01-4322, 02-1220] [1465052-1] (amyd) [01-4316 01-4317 01-4318 01-4319 01-4320 01-4321 01-4322 02-1220]

DATE	ENTRY
7/24/03	ORDER: Final judgment filed per opinion. Petitioners-appellants to pay costs. [01-4316, 01-4317, 01-4318, 01-4319, 01-4320, 01-4321, 01-4322, 02-1220] [0-0] (amyd) [01-4316 01-4317 01-4318 01-4319 01-4320 01-4321 01-4322 02-1220]
9/8/03	Filed 30c Petition for Rehearing and Petition for Rehearing Enbanc by Appellant Estate Burton Kanter in 01-4316, Appellant Estate Burton Kanter in 01-4317, Appellant Estate Burton Kanter in 01-4318, Appellant Estate Burton Kanter in 01-4319, Appellant Estate Burton Kanter in 01-4320, Appellant Estate Burton Kanter in 01-4321, Appellant Estate Burton Kanter in 01-4322, Appellant Naomi R. Kanter in 02-1220. Dist. [01-4316, 01-4317, 01-4318, 01-4319, 01-4320, 01-4321, 01-4322, 02-1220] [1658913-1] (tiff) [01-4316 01-4317 01-4318 01-4319 01-4320 01-4321 01-4322 02-1220]
10/21/03	ORDER: Appellant Estate Burton Kanter in 01-4316, Appellant Estate Burton Kanter in 01-4317, Appellant Estate Burton Kanter in 01-4318, Appellant Estate Burton Kanter in 01-4319, Appellant Naomi R. Kanter in 01-4320, Appellant Estate Burton Kanter in 01-4320, Appellant Estate Burton Kanter in 01-4321, Appellant Estate Burton Kanter in 01-4322, Appellant Naomi R. Kanter in 02-1220 Petition for Rehearing and Petition for Rehearing Enbanc is DENIED. [01-4316, 01-4317, 01-4318, 01-4319, 01-4320, 01-4321, 01-4322, 02-1220] [1658913-1] (tiff) [01-4316 01-4317 01-4318 01-4319 01-4320 01-4321 01-4322 02-1220]

DATE	ENTRY
10/29/03	MANDATE ISSUED AND ENTIRE RECORD RETURNED WITH BILL OF COSTS IN THE AMOUNT OF $114.40. (Contents returned: 44 vol. pleadings; 3 exhibits.) [01-4316, 01-4317, 01-4318, 01-4319, 01-4320, 01-4321, 01-4322, 02-1220] [1597404-1] (amyd) [01-4316 01-4317 01-4318 01-4319 01-4320 01-4321 01-4322 02-1220]
4/26/04	Filed order from the Supreme Court GRANTING the Petition for Writ of Certiorari. Supreme Court Case No.: 03-1034. [01-4316, 01-4317, 01-4318, 01-4319, 01-4320, 01-4321, 01-4322, 02-1220] [1756190-1] (jame) [01-4316 01-4317 01-4318 01-4319 01-4320 01-4321 01-4322 02-1220]

UNITED STATES TAX COURT

CLAUDE M. BALLARD AND BURTON W. KANTER,

v.

C.I.R.,

Consolidated Docket Nos.
43966-85, 712-86, 45273-86, 1350-87, 31301-87, 33557-87, 3456-88, 30830-88, 32103-88, 27444-89, 16421-90, 25875-90, 26251-90, 20211-91, 20219-91, 21555-91, 21616-91, 23178-91, 24002-91, 1984-92, 16164-92, 19314-92, 23743-92, 26918-92, 7557-93, 22884-93, 25976-93, & 25981-93

DOCKET ENTRIES

DATE	EVENT	FILINGS AND PROCEEDINGS
01/09/86	PF	PETITION Filed: Fee Paid
07/14/87	OAJ	ORDER that case is assigned to Judge Williams.
07/18/90	ORJ	ORDER that case is reassigned to Judge Halpern.
01/07/94	ORJ	ORDER that case is reassigned to Judge Covillion.
01/14/94	O	ORDER set 6/13/94 Chicago, IL (Spec.) for trial. All mots. by any party to be filed by 5/23/94.

DATE	EVENT	FILINGS AND PROCEEDINGS
06/13/94	PTRL	PARTIAL TRIAL before S.T. Judge Couvillion at Chicago, IL Also called 6/14, 15, 16, 17, 20, 21, 22, 23 & 24. Resp's amendment to answer filed & served 6/13/94 (see below). Petrs' reply to amendment to answer filed & served 6/13/94 see below). Declaration by third party Solomon Weisgal filed 6/13/94 (see below). Resp's 5 mots. to compel compliance with subpoenas filed 6/20/94—Dn. (see below). Continued for further trial—SEE ORDER. NO BRIEFS DUE.
07/25/94	FTRL	FURTHER TRIAL before S.T. Judge Couvillion at Chicago, IL
02/14/95	O	ORDER record is closed.
05/15/95	BFR	BRIEF for resp. (Leave Gr.)
05/15/95	BFP	BRIEF for petr. (Leave Gr.)
12/15/99	ORJ	ORDER that case is reassigned to Judge Dawson.
12/15/99	MOP5	MEMORANDUM OPINION, Judge Dawson T.C. Memo 1999-407 (adopting opinion of S.T. Judge Couvillion). (Decisions in all dockets will be entered under Rule 155.)
01/24/00	O	ORDER mot. to ext. time is gr. in that time ext. to 5/15/00 for all parties to file any mot. for recons. & supporting memo. (Special instructions including limit on no. of pages in mot. & memo.) Parties by 3/15/00 file memorandum report.

DATE	EVENT	FILINGS AND PROCEEDINGS
04/20/00	MOTP	MOTION by petr. for access to original special trial judge report prepared under Rule 183(b), including request for interlocutory appeal & request that materials be made part of the record. (C/S 4/19/00) (Leave Gr.)
04/20/00	MEMO	MEMORANDUM OF POINTS & AUTHORITIES by Petrs. in support of mot. for access to original special trial judge report, etc. (C/S 4/19/00) (Leave Gr.)
04/26/00	O	ORDER Petrs' mot. for access to original special trial judge report, including request for interlocutory appeal & request that materials be made part of the record, is dn.
05/03/00	MOTP	MOTION by petr. for ext. of time to file mot. for recons. of opinion. (C/S 4/27/00)
05/04/00	O	ORDER Petrs' mot. to ext. time to file mot. for recons. is gr. in that time ext. to 6/2/00.
05/23/00	MOTP	MOTION by petr. to ext. time to 7/3/00 to file mot. for recons. (C/S 5/22/00)
05/26/00	MOTP	MOTION by petr. to place original special trial judge report under seal & made part of record for review by circuit court of appeals. (C/S 5/25/00) (per Judge)
07/31/00	MEMO	MEMO MEMORANDUM OF POINTS & AUTHORITIES by Petr. Kanter in support of mot. to reopen record & for recons. (per Judge)

DATE	EVENT	FILINGS AND PROCEEDINGS
08/22/00	MOTP	MOTION by petr. to reconsider Court's denial of Petrs' mot. for access to original special trial judge report prepared under Rule 183(b) or, in the alternative, for new trial. w/Ex. (C/S 8/21/00) (per Judge)
08/30/00	O	ORDER Petrs' mot. to reconsider Court's denial of Petrs' mot. for access to original special trial judge report or for new trial is dn.
12/05/00	MOTP	MOTION by petr. to stay entry of decision until ruling on Petrs' ORD 12/21/00 petition for writ of mandamus in Court of Appeals. (C/S 12/4/00)
12/21/00	O	ORDER Petrs' mot. to stay entry of dec. is dn. w/Exs. att'd
09/24/01	DEC	DECISION ENTERED, Judge Dawson
12/14/01	NOAP	U.S.C.A., 7th Cir. C/S 12-13-01. FEE PAID. (petr. Estate of Burton W. Kanter, Dec'd., Joshua S. Kanter, Executor) C.A.#01-4316.
12/26/01	NOAP	NOTICE OF APPEAL by petr. To U.S.C.A., 11th Cir. FEE PAID. C.A.#01-17251-I

U.S. TAX COURT

DOCKET NUMBER: 43966-85, 712-86, 45273-86, 1350-87, 31301-87, 33557-87, 3456-88, 30830-88, 32103-88, 27444-89, 16421-90, 25875-90, 26251-90, 20211-91, 20219-91, 21555-91, 21616-91, 23178-91, 24002-91, 1984-92, 16164-92, 19314-92, 23743-92, 26918-92, 7557-93, 22884-93, 25976-93, 25981-93

In The Matter of:

INVESTMENT RESEARCH ASSOCIATES, LTD., AND SUBSIDIARIES, *et al.*,

Petitioners,

vs.

COMMISSIONER OF THE INTERNAL REVENUE,

Respondent.

Volume I

Pages: 1-260

Location: Chicago, Illinois

Date: June 13, 1994

On The Record Reporting, Inc.
5926 Balcones Drive, Suite 115
Austin, Texas 78731
(521) 450-0342

[420] Q That is the—the bank where the check was ultimately cashed imprints that number on there. Now, on -37 there is no such number on the lower right-hand corner. Do you see that?

A Yes.

Q So it means that the copy of this check was made before the check was negotiated, since there is no bank number in the lower right-hand corner. Do you know why it is that one of the checks that you sent to the government was a check that came after negotiation and one was a check that was photocopied by you before negotiation?

A I would have no idea.

Q You have no idea? I would imagine this must have been done by somebody in your office?

A Don't know. Have no idea.

Q Now, Mr. Schaffel, to your knowledge, did Robert Lisle or Claude Ballard ever use any influence to obtain business for you, any persons or entities with which you were in business, at either Prudential Insurance Company or Travelers Insurance?

A No.

Q Did you ever intend to compensate either Claude Ballard or Robert Lisle for any business that you or any entity or persons with whom you were in business at either Prudential Insurance Company or Travelers?

A Never.

Q And do you have any knowledge of any payments to either Mr. Ballard or Mr. Lisle by virtue of any business that you or any person or entity with whom you were in business at Prudential Insurance Company or Travelers Insurance?

A No.

MR. MARTIN: I have nothing further.

THE COURT: Mr. Dick?

MR. DICK: I just have one brief question.

CROSS-EXAMINATION

BY MR. DICK:

Q. Now, you discussed the One River Associates and I think you testified that that was not a Prudential or a Travelers deal. Is that correct?

A Yes.

Q Okay. And that was from a savings bank name of?

A The financing was created by the Howard Savings Bank as a joint venture.

Q So neither—

A And the lender was New York Life.

Q Okay. And neither Prudential Nor Travelers had any relationship with these.

* * * *

FREY - DIRECT [713]

examine? Mr. Martin?

CROSS-EXAMINATION

BY MR. MARTIN:

Q Mr. Frey, is it true that Mr. Kanter introduced You to Mr. Ballard for the purpose of causing Mr. Ballard -- for the purpose of influencing Mr. Ballard to do business with you?

A I don't recall that.

Q To your knowledge—

A I would say no.

Q To your knowledge, did Mr. Ballard ever use any influence to obtain business for you at the Prudential Insurance Company?

A Absolutely not. The business we got was on the merits.

Q Did you ever intend to compensate Mr. Ballard for any business that you did with Prudential?

A Absolutely not.

Q And do you have any knowledge of any -. compensation received by Mr. Ballard by virtue of business that you or your entities did with Prudential?

A Absolutely not.

MR. MARTIN: That is all I have got.

[714] FREY - CROSS

CROSS-EXAMINATION

BY MR. BROWN:

Q I will ask you similar questions for Mr. Lisle. To your knowledge, did Robert Lisle ever use any influence to obtain—

MR. DECATOR: Objection, Your Honor. This is beyond direct. We never even discussed Mr. Lisle in any way.

THE COURT: Well, the witness is on cross-examination. However, I do agree with you. I don't think Mr. Lisle's name was ever brought up on direct. But I think you could ask him whether or not he had any contact or knew Mr. Lisle.

BY MR. BROWN:

Q Have you ever met Mr. Robert Lisle?

A I don't believe so. He—after he left Prudential, he was at Travelers, and we went to Travelers one day. I don't think I am not sure we met him or not. we do.

Q Well, then, I will ask you the question. To your knowledge, did Robert Lisle ever use any influence to obtain business for you, any persons or entities with whom you were in business, either at Prudential or at Travelers?

A Absolutely not.

FREY – CROSS [715]

Q Did you ever intend to compensate Mr. Lisle, Mr. Robert Lisle, for any business that you or any entity or

persons with whom you were in business at either Prudential Insurance Company or Travelers Insurance Company—

A Absolutely not.

Q Do you have any knowledge of any payments to either—to Mr. Robert Lisle by virtue of any business that you or any person or entity with whom you were in business at either Prudential Insurance Company or Travelers Insurance Company?

A Absolutely not.

MR. BROWN: No more questions.

THE COURT: Mr. Dick?

MR. DICK: Yes, Your Honor. Just one minute.
(Pause.)

CROSS-EXAMINATION

BY MR. DICK:

Q I am going to hand you what has been entered into evidence as Exhibit 458 and direct your attention to page 2 of that document.

A Yes.

Q And I know this is hard to read, but in paragraph 6, it says, "The contribution of each limited partner is as follows." Do you see that?

* * * *

SCHNITZER - CROSS [2188]

But if I was to tell you that if Mr. Ballard or Mr. Lisle had ever been asked to intervene, that would have been the quickest way f o r us to have lost the regional business.

It is not—they could never help you. They could hurt you. And I am sure that if they didn't—wouldn't have wanted us to have the business, we couldn't have had it. But they sure as hell couldn't have gotten it for us and allowed us to keep it.

Q Now, who on the PMS side would do the negotiating with these regional people from insurance companies and other people?

A Most of the time it was done at a very senior level, but originally a man by the name of Burrows—Roland Burrows; following that, a man by the name of Joe Hudec, who was president. But they always worked with our regional person involved in that particular territory. So it was—but it required a very senior person to be dealing with that kind of—

Q So Mr. Hudec or Mr. Burrows, during the '70s, would have been doing this negotiation.

A Yes, sir.

Q And PMS did a good job, and that is why they are continuing to get business.

A Correct.

* * * *

SCHNITZER - CROSS [2192]

Q And you have had—oh, gosh—two or more conversations with them in preparation for this morning?

A Yes, sir.

Q Did they ever ask you during any of those interviews whether or not you ever made a payoff or bribe of any kind to Mr. Lisle or Mr. Ballard?

A I don't think they asked that. They asked me if I knew that—

Q Did they ask you whether or not you had ever paid them for any influence at Prudential or Travelers?

A I don't recall, to be honest with you.

Q To your knowledge, did Mr. Lisle or Mr. Ballard ever use any influence to obtain business for you either—or any persons with whom you were in business at either Prudential Insurance Company or Travelers Insurance Company?

A No, sir.

Q Did you ever intend to compensate these—either Mr. Ballard or Mr. Lisle for any business that you or any entity or

persons with whom you were in business at either Prudential Insurance Company or Travelers Insurance Company?

A No, sir.

Q Do you have any knowledge of any payments to either Mr. Ballard or Mr. Lisle by virtue of any business

* * * *

[2216]

of things. And apparently that—apparently you have not been advised of those kind of things.

MR. DICK: No, Your Honor.

MR. COMEAU: Judge—

MR. DICK: All we did is receive 4,000 checks from the Respondent. And Respondent's position has always been, Well, we have them; they are somehow relevant; stipulate to them. And we have consistently said, No, we are not. Tell us what is important in each check, why you would like it, and then we will discuss it.

And we have also said, Judge, if it relates to IRA, TMT, BWK, Carlco, or Mr. Schaffel or any of these entities, obviously they are relevant. The rest are not relevant.

THE COURT: But volume-wise, how much are we looking at?

MR. DICK: 2,000 pieces of paper.

THE COURT: 2,000 pieces of paper?

MR. DICK: At least—which I had to look for the ones before.

MR. BROWN: Some of which are made out to Xerox Company and—

THE COURT: It strikes the Court that somehow or another Respondent is attempting to throw the audit process into the

Court's hands, and the Court is not [2217] willing to do an audit.

MR. COMEAU: We are not willing to—

THE COURT: As Respondent well knows, we don't do audits.

MR. COMEAU: We are not willing—we are not suggesting that.

THE COURT: Well, when you start talking about 2,000 exhibits—

MR. COMEAU: When we have ten years, Judge.

THE COURT:—besides what—besides everything else that has been presented to the Court, I don't know.

MR. COMEAU: Well, if the problem—if the method of proof the Government is using to show the money flowing through would be a source-and-application-of-funds method of proof, or if this was a bank deposit case, where you are trying to prove admitted income through a bank deposit case, all deposits to that account or checks withdrawn from those accounts, even if they may be checks to Commonwealth Edison for a utility bill, would be documents that would be relevant in this case.

THE COURT: That is correct, but that is a different matter together. When you are applying an indirect method of income, that is because when Respondent determines that the books and records are not adequate to [2218] determine the taxpayer's income.

MR. COMEAU: Right.

THE COURT: But this is a totally different matter. I don't think Respondent has ever claimed that there were no books and records kept from which income could be determined.

MR. COMEAU: No, we are not. But—

THE COURT: You are claiming fraud.

MR. COMEAU: We are claiming the monies went directly Right.

THE COURT: And you are claiming fraud, and when you start saying—when you start dumping 2,000 documents and saying, All right, the fraud is all in this—

MR. COMEAU: No. But my point is, to adequately trace the money through the various bank accounts, you need the deposits and the withdrawals. Now, if we just had—they said IFI is not a Petitioner in this case. Well, there are non-related Petitioners: IFI—

THE COURT: Well, I understand that—that were corporations of Mr. Kanter. I understand that. I don't have any problem with that, if money has flowed through IFI and whatever else—IFC and whatever.

MR. COMEAU: The Holding Company, a number of

* * * *

[2220]

MR. COMEAU:—because there is no witness that may have said there is a conspiracy, but the money will show it.

MR. BROWN: Here we go. Okay. NOW, what does a check to American Express or a check to Amoco [phonetic] have to do with this case? That is what the counsel—

THE COURT: That is my concern.

MR. BROWN: Exactly.

MR. COMEAU: Well, we will take the checks—

THE COURT: If you can come up with specific—checks for—on which you are basing your case that those matters definitely will be introduced into evidence. But I am

concerned over a conglomeration of checks, and I led to believe that that is what we are looking at here.

MR. DICK: It is.

MR. BROWN: Yes, Your Honor.

MR. DICK: And that is only for one year. 2,000 checks for one year, and we have ten years here. We are talking about 20,000 checks.

THE COURT: If there was fraud involved—and I am not saying that there was or there wasn't—I haven't heard all the evidence. But it seems to me that unrelated checks certainly would not help your case at all. If anything, they probably hurt your case, really.

To be honest, if you want to establish fraud, you better specify and come down to specifics and don't throw a bunch of documents at me, because then—you know, I am human, too, and I will certainly give a lot more attention to something if you can come up with specific transactions and trace it through.

Just because it is IFI, and even though IFI is not a litigant in this case, that is not what I am looking at. But 2,000 exhibits on a lot of checks that admittedly are unrelated to his and are even unrelated to any kind of fraud—payments to Amaco or whatever—unless you can show that a payment to Amaco was for the benefit of Mr. Kanter individually or whatever—I don't know.

But at this point, I think the objection is well taken to those exhibits.

MR. COMEAU: Okay. Then, at this point—

THE COURT: You know, you have got plenty of time left, you know, to put these documents in order.

MR. COMEAU: Okay. Then with that I lost this argument—you are right. I understand. I have an argument why I want them in. You have ruled.

THE COURT: That is correct.

MR. COMEAU: With this ruling in mind and the predicament that it now places me in at this stage of the trial, with no records that we—of the ones we do need in, instead of sitting here for the rest of the afternoon,

* * * *

[2332]

both sides have very strong feelings about their cases, but you have got to understand that the Court is a third party in this.

MR. DICK: I agree.

THE COURT: And the Court, you know, has rules to go by.

And I don't think either side is being fair to their clients. I am not—you know, maybe I am being critical and maybe I shouldn't be, but, you know—

MR. DICK: Well, I think you are being critical and you should be, Judge.

THE COURT:—the cases are not being presented in a fashion that lawyers who are skilled and schooled in tax law should know about. And I don't know who is really to blame for all that. But all I can say is both sides seem to me have blocked off any communications with each other.

And here we are drifting along, and I don't know where the hammer is going to fall, but it is going to fall at a certain point in time, and somebody will not have presented their case.

MR. DICK: Well, it certainly will not be the Petitioners, Your Honor.

THE COURT: Well, it may be.

MR. DICK: We are ready to go, Judge. We really are.

* * * *

CONNOLLY - CROSS [2669]

that came to you as Gateway was a result of the management fee that you earned under the contract with Prudential.

A That is correct.

Q And you gave a part of that management fee away to, in essence, MHM and other partners in Essex to get you all the support services that you must have had in order to keep the contract with Hilton—

A That is correct.

Q —with Prudential. Excuse me. And the reason for the participation of John Formby in Essex and the reason for your relationship with Formby was because of his position with MHM. Right?

A That is correct.

Q He was the in-house financial person for MHM. Right?

A That is correct.

Q And he then became your financial person for Gateway.

A That is correct.

Q And that is because of this Essex partnership. Right?

A That is correct.

Q. Through the payments that Gateway, your company made to Essex, the partnership, the 80 percent of the management—75 percent of the management fee

[2670] CONNOLLY - CROSS

according to the contract—through those payments did you ever intend to compensate Claude Ballard or Bob Lisle for exercising their influence to get you any management contract?

A Absolutely not.

Q To your knowledge, did either Claude Ballard or Bob Lisle have anything to do with your obtaining those two hotel contracts?

A No.

Q And in fact, isn't it true that at the time that you obtained the Midland Hotel contract, Claude Ballard was already gone from The Prudential?

A That is correct.

MR. MARTIN: I have nothing further.

THE COURT: Mr. Dick?

MR. DICK: No, Your Honor.

THE COURT: No further cross-examination.

Any redirect, Ms. Gibson?

MS. GIBSON: One moment, Your Honor. We have no further redirect.

THE COURT: All right. I believe that would conclude your testimony, Mr. Connolly.

THE WITNESS: Thank you, Your Honor.

THE COURT: Thank you.
(Whereupon, the witness was excused.)

* * * *

we put on rebuttal that this evidence is being introduced with respect to the Prudential schemes and any of the non-Prudential issues and amended answers have been stricken.

THE COURT: Oh, I see what you mean. Right. I have already stricken that. That is correct.

MR. DICK: So this has to do with the Prudential.

THE COURT: But I think Respondent would bear the burden on that too.

MR. DICK: I agree.

THE COURT: So your burden would be to show that this income is not related—is related to the Prudential five, or to the Prudential scheme, or "The Five." I might learn all this after a while.

MR. MARKLEY: We know what you mean, we understand.

THE COURT: Are we understood here?

MR. MARKLEY: We understand, yes.

THE COURT: So I will allow the documents if that what those documents purport to show.

MR. MARKLEY: That is what we would represent that they purport to show.

THE COURT: But I want you to understand the questions that Petitioners are raising. Just because you put the check in the record does not necessarily establish

your proof; it may or it may not.

MR. MARKLEY: I certainly have had a lot of trials where I put lots of evidence in and it didn't prove anything.

THE COURT: All I know is I am not the attorney, I haven't been working on this three, four, five or ten years that you all have been working on it, so please understand, just being hit cold I can't decipher among all the various entities and trusts and whatever.

MR. MARKLEY: Judge, we understand that when you throw notebooks down the stairs, the heaviest one to the bottom isn't necessarily the best. We understand that, and that is not what we are saying. We are saying we need to get it in to be

able to argue that something is worthwhile in there, and we understand that.

THE COURT: All right. I don't know whether this is an appropriate expression to make, but I believe Yogi Berra made the expression that you can observe a lot just by looking. So I want to be able to look so that I can observe and conclude what we have.

MR. MARKLEY: He also said, It is deja vu all over again.

THE COURT: I don't know that Yogi Berra did all these things, but he is getting a lot of credit for things that do make a lot of cornfield sense.

UNITED STATES TAX COURT

Certificate of Transcriber and Proofreader

CASE NAME: Investment Research Associates Inc., *et al.*

DOCKET NUMBER: 43966-85, *et al.*

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Supreme Court, U.S.
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No. 03-1034

IN THE

Supreme Court of the United States

ESTATE OF BURTON W. KANTER, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ON WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTIONS PRESENTED

The Tax Court keeps secret, even from the reviewing courts of appeals, the findings of fact and credibility judgments of its Special Trial Judges. By law, these trial judges are required after trial to submit reports to the Tax Court that contain the trial judge's findings of fact and opinion. Tax Ct. R. 183(b). By law, these findings of fact of the trial judge "shall be presumed to be correct" by the Tax Court and the Tax Court must give "due regard" to the trial judge's "opportunity to evaluate the credibility of witnesses." Tax Ct. R. 183(c). Nonetheless, the Tax Court overturns the factual findings of its trial judges, including their credibility findings, without revealing those findings to the parties or reviewing courts of appeals; without offering any reasons for rejecting those findings; and without even disclosing that the Tax Court has rejected those findings. Secret trial judge reports preclude the courts of appeals from engaging in proper appellate review. Federal statutes require that "all reports of the Tax Court * * * shall be public records." 26 U.S.C. §7641(a). The questions presented are:

1. Whether the due process clause or the governing federal statutes requires that the courts of appeals be able to review Tax Court decisions on the basis of the complete record, including the trial judge's findings of fact that, by law, the Tax Court must presume to be correct.

2. Whether Tax Court Rule 183 requires judges of the Tax Court to uphold findings of fact and credibility judgments made by their trial judges, unless those findings are "clearly erroneous," as the D.C. Circuit has held, or whether those findings and credibility judgments are entitled to no deference at all, as the Seventh Circuit held in this case.

RULE 14.1(b) STATEMENT

The following are the parties to the proceeding in the Court of Appeals for the Seventh Circuit:

1. Estate of Burton W. Kanter, Deceased
2. Joshua S. Kanter, as Executor of the Estate of Burton W. Kanter
3. Naomi Kanter
4. Commissioner of Internal Revenue, United States Department of the Treasury

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a to 97a) is reported at 337 F.3d 833 (7th Cir. 2003). The opinion of the Tax Court (Pet. App. 98a) is reported at 78 T.C.M. (CCH) 951 (1999). The orders of the United States Tax Court (Pet. App. 99a-112a) denying access to the Special Trial Judge's Rule 183 Report are unreported.

JURISDICTION

The judgment of the court of appeals was entered on July 24, 2003. A timely petition for rehearing was denied on October 21, 2003. Pet. App. 115a. A timely petition for a writ of certiorari was granted on April 26, 2004. This Court's jurisdiction rests on 28 U.S.C. § 1254(1).

CONSTITUTIONAL PROVISIONS, STATUTES AND RULES INVOLVED

The relevant constitutional provisions, statutes, and rules are set forth at Pet. App. 116a to 121a.

INTRODUCTION

The questions presented here concern whether the Tax Court may insulate its decisions from proper appellate review by keeping secret the findings of fact of its trial judges. The Tax Court is legally obligated to presume these findings to be correct, but refuses to disclose them to the parties or the reviewing courts. A divided panel of the court of appeals determined that neither due process nor the relevant statutes obligated the Tax Court to disclose the legally-required findings of fact and opinion of the trial judge who presided over 28 days of live testimony, involving 60 different witnesses, at the trial of this case. It is undisputed that the Tax Court reached its ultimate decision – finding tax fraud and imposing over 30 million dollars of liability – only after reversing critical findings of fact, including credibility judgments, of the judge who had tried the case. The Tax Court's opinion not only provides no reasoned explanation

for this reversal; it contains no acknowledgement that the Tax Court reversed these findings at all. The trial judge's original Report has never been disclosed to the parties or to the reviewing courts.

STATEMENT

1. Structure of the Tax Court. Congress established the United States Tax Court as an Article I "court of record." 26 U.S.C. § 7441. "The Tax Court's function and role in the federal judicial scheme closely resemble those of the federal district courts." *Freytag* v. *Comm'r*, 501 U.S. 868, 891 (1991). The Tax Court is an Art. I court whose sole function is the adjudication of tax disputes; it has no prosecutorial, investigative, or substantive rule-making powers. *Id.* at 890-91 (holding that Tax Court exercises only "judicial, rather than executive, legislative, or administrative power"); see also *id.* at 912-13 (Scalia, J., dissenting) (characterizing Tax Court as located in executive branch but engaged only in adjudication). In constituting the Tax Court as an Article I court in 1969, Congress granted the Tax Court additional judicial powers, such as the power to punish contempt, and completed the process of transforming the Tax Court from an executive agency into a full judicial institution. See generally H. Dubroff, THE UNITED STATES TAX COURT: AN HISTORICAL ANALYSIS 204-17 (1979); *id.* at 213 (noting applicability of Administrative Procedure Act to Tax Court was unsettled before 1969).

Tax Court decisions, like district court judgments, can be appealed only to the courts of appeals, with ultimate review in this Court. *Freytag*, 501 U.S. at 891. Congress also specifically legislated to require the courts of appeals to review decisions of the Tax Court "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury." 26 U.S.C. § 7482(a); see *Comm'r* v. *Duberstein*, 363 U.S. 278, 291 n.13 (1960) (purpose of 26 U.S.C. § 7482(a) was to overrule earlier Court

decision and ensure that Tax Court findings of fact are reviewed just as intensively as District Court findings). See also *Freytag*, 501 U.S. at 891 ("This standard of review contrasts with the standard applied to agency rulemaking by the courts of appeals under §10(e) of the Administrative Procedure Act, 5 U. S. C. § 706(2)(A).").

In somewhat similar fashion to the way the District Courts are permitted to appoint magistrates, see 28 U.S.C. §631, the chief judge of the Tax Court "may, from time to time, appoint special trial judges * * *." 26 U.S.C. §7443A(a).[1] The Chief Judge may assign any proceeding for trial to a Special Trial Judge, "regardless of complexity or amount." *Freytag*, 501 U.S. at 873; see also 26 U.S.C. §7443A(b). The consent of the parties is not required. The Tax Court thus has plenary power to decide which cases are tried to Special Trial Judges.

Special Trial Judges ("STJs" or "trial judges") are "judicial officer[s]." See Tax Ct. R. 3(d). By statute, their salaries are 90% of those of Tax Court judges. 26 U.S.C. §7443A(d)(1). The STJs exercise a portion of the Tax Court's adjudicative function and possess the considerable powers associated with that function:

> They take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders. In the course of carrying out these important functions, the special trial judges exercise significant discretion.

Freytag, 501 U.S. at 881-882. See Tax Ct. R. 181 (STJs conduct trials, issue subpoenas, command production of evidence, rule on motions, conduct pretrial hearings, rule on

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[1] Special Trial Judges are at-will employees appointed at the discretion of the Chief Judge. They have no statutory term of office and serve at the pleasure of the Tax Court. See 26 U.S.C. § 7443A.

evidentiary questions, and conduct similar proceedings). In several types of proceedings, Congress has authorized these trial judges to issue the final opinion of the Tax Court. 26 U.S.C. §7443A(c). As this Court has recognized, Special Trial Judges exercise such "significant governmental authority" that they are "inferior Officers" of the United States whose appointment must comply with the requirements of Article II of the Constitution. 501 U.S. at 880-882.

The financially most significant cases the Tax Court may assign for trial to these judges, such as this one, involve claimed deficiencies that exceed $50,000. Such cases, when tried to a Special Trial Judge, are governed by the special procedures set forth in Tax Court Rule 183. Under that Rule, the Special Trial Judge conducts the trial and is legally required to make recommended findings of fact. After the trial and post-trial briefing, the Special Trial Judge must "submit a report, including findings of fact and opinion" to the Chief Judge. Tax Ct. R. 183(b). The Chief Judge then assigns a Tax Court Judge to review this Rule 183 Report. *Id.* Rule 183(c) provides: "The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions." Tax Ct. R. 183(c).

Rule 183 requires that, in exercising his power to reach final decision, the Tax Court judge is constrained by the requirement that he "shall" presume correct the trial judge's factual findings and that he "shall" defer to the trial judge's opportunity to hear the witnesses:

> "*Due regard* shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the

> findings of fact recommended by the Special Trial Judge *shall be presumed to be correct.*"

Tax Ct. R. 183(c) (emphasis added.)

The Tax Court acknowledges that this Rule requires deference to the trial judge's judgments of credibility and findings of fact. See Pet. App. 108a (Tax Court order denying access to STJ findings but proclaiming that those findings were, in fact, accorded the required deference). Prior to the decision below, the D.C. Circuit, the only court to have squarely ruled on the issue, had long held, and the Tax Court bar had long understood, Rule 183(c) to mean that the Special Trial Judge's findings of fact are to be overturned only if clearly erroneous. See, *e.g.*, *Landry* v. *FDIC*, 204 F.3d 1125, 1133 (D.C. Cir. 2000); *Stone* v. *Comm'r*, 865 F.2d 342, 345 (D.C. Cir. 1989); 35 AM. JUR. 2d *Fed. Tax Enforcement* § 905 (2002) ("The Tax Court is required to review a special trial judge's factual findings according to the clearly erroneous standard."); 20A FEDERAL PROCEDURE, L. ED., INTERNAL REVENUE § 48:1274 (2000) (same).

2. The Tax Court's Secret Process of Decision-making.

a. This case arises because the Tax Court, in a reversal of a policy that had governed for over 40 years, now takes the position that it will keep *legally binding* findings of fact of its trial judges completely secret, including from the Article III appellate courts legally required to review the Tax Court's decisions. Even in a civil tax fraud case where credibility findings are critical, neither the taxpayer, nor the government, nor the court of appeals – even *in camera* – are permitted to see the trial judge's Rule 183 report or to review the full record underlying the Tax Court's decision. As Judge Cudahy observed below, the Tax Court is "unique among all the institutions in the law" in claiming the power to refuse to disclose the "presum[ptively] correct" findings of fact of a trial judge. Pet. App. 71a.

Even in the Tax Court this procedure is relatively new. The Tax Court adopted this secretive process only by abandoning a longstanding, transparent one. Long before the Tax Court became an Article I court of record, and long before the office of Special Trial Judge was created, Congress in 1943 first granted the Tax Court power to use "commissioners" – predecessors to Special Trial Judges – to try cases. Revenue Act of 1943, ch. 63, Sec. 503(b), 58 Stat. 72. The Tax Court in 1944 immediately promulgated Rule 48 which required that the commissioner's report be served on the parties and that the parties be permitted to file exceptions to the commissioner's findings before the Tax Court issued its final decision. Tax Ct. R. 48(c) (July 1, 1944 ed.).

This structure, including disclosure and the right to file exceptions, was carried forward in later Tax Court rules as the Tax Court changed the title of "commissioners" to "Special Trial Judges," increased the judicial powers of these trial judges, and turned the STJ into a "judicial officer." See former Tax Ct. R. 182(b), 60 T.C. 1149 (1973) (providing for service of the Special Trial Judge's report on each party and allowing each party to file objections to the report's findings); Tax Ct. R. 3(d). Until 1983, Tax Court Rules *required* routine disclosure in every case of the Special Trial Judge's report *and* provided the right to file exceptions.

In 1983, that changed when the Tax Court amended its rule in only one, odd respect: it eliminated mandatory, routine disclosure of the trial judge's report. See 81 T.C. 1069 (1983) (amending Rule 182 and renumbering it as Rule 183). The Tax Court changed nothing else about the trial judge or the Tax Court's role: the amended rule continued to require, in the exact same terms, that the Tax Court give "due

regard" and "presumed . . . correct" deference to the Special Trial Judge's findings of fact.[2]

The Tax Court has never offered any explanation for this 1983 amendment to its longstanding, consistent practice of disclosure. The Tax Court, unlike the federal courts or administrative agencies, employs no notice-and-comment process for issuing its rules of procedure. Indeed, it appears to have no formal process at all for issuing rules. Like the use of secret STJ reports, this lack of any formal process for promulgating rules of procedure is, as Judge Cudahy noted below, "oddly out of sync with prevailing practices in other areas of the law." Pet. App. at 77 n.2.[3] Taxpayers and

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[2] The language governing the Tax Court's review of the reports of Special Trial Judges had been contained in Tax Court Rule 182(d), which provided:

> (d) **Oral Argument and Decision**. The Division to which the case is assigned may, upon motion of any party or on its own motion, direct oral argument. The Division inter alia may adopt the [Special Trial Judge's] report or may modify it or may reject it in whole or in part, or may receive further evidence, or may recommit it with instructions. Due regard shall be given to the circumstance that the [Special Trial Judge] had the opportunity to evaluate the credibility of witnesses; and the findings of fact recommended by the commissioner shall be presumed to be correct.

Tax Ct. R. 182(d), 60 T.C. 1150 (1973). The 1983 amendments "renumbered [Rule 182(d)] as Rule 183(c), but the last sentence is unaltered." *Stone* v. *Comm'r*, 865 F. 2d 342, 345 (D.C. Cir. 1989).

[3] See 28 USC § 2071(b) ("Any rule prescribed by a court, other than the Supreme Court, under subsection (a) shall be prescribed only after giving appropriate public notice and an opportunity for comment."); Fed. R. App. P. 47(a)(1) ("Each court of appeals acting by a majority of its judges in regular active service may, after giving appropriate public notice and opportunity for comment, make and amend rules governing its practice."); Fed. R.

reviewing courts can therefore only guess at the reasons for the 1983 change.[4]

The note that accompanied the amendment simply states that "the prior provisions for service of the [Special Trial Judge's] report on each party and for the filing of exceptions to that report have been deleted." Tax Ct. R. 183, 81 T.C. 1070 (adopted 1983). An accompanying press release also announced without explanation that "[t]he Special Trial Judge's report will not be served on the parties automatically, nor will the parties automatically be given an opportunity to file additional briefs setting forth exceptions to that report." United States Tax Court Press Release, January 10, 1984, reprinted in U.S. Tax Week, 1984 No.2, page 81, January 13, 1984.

b. The current Tax Court process is even more remarkable than the "mere" non-disclosure of the trial judge's original findings. As the government now concedes, the Tax Court employs a procedure that makes it impossible for anyone, including the parties, the reviewing court of appeals, or this Court, to determine whether the Tax Court has overturned the findings, including the credibility findings, of the judge who tried the case – and if so, why.

In every reported decision since the 1983 disclosure repeal, the final decision of the Tax Court begins with a

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Civ. P. 83(a)(1) (a district court must "giv[e] appropriate public notice and an opportunity for comment" before making and amending local rules).

[4] This change was made during pendency of a highly visible case in which the Tax Court had publicly reversed the findings of its trial judges, only to be later reversed by the D.C. Circuit for giving insufficient deference, under its own rules, to the trial judge's findings. See *Rosenbaum* v. *Comm'r*, 45 T.C.M. (CCH) 825 (1983), *rev'd sub nom. Stone* v. *Comm'r*, 865 F.2d 342 (D.C. Cir. 1989).

boilerplate statement that the Tax Court judge "agrees with and adopts the opinion of the Special Trial Judge." See Pet. App. 3a, 98a (emphasis added). Following that statement is an opinion issued in the name of the Special Trial Judge. "[T]here exists not a single Tax Court decision since the adoption of current Rule 183 where a Tax Court Judge has purported to modify or reverse a finding of a Special Trial Judge." Pet. App. 73a.

As the government now concedes, that boilerplate language does not mean that the final "opinion" is the same as the Rule 183 "report" with its original findings of fact intact. See Gov't Br. in Opp'n, *Ballard v. Comm'r* ("*Ballard* Opp."), No. 03-184, at 13 n.3 (filed Oct. 6, 2003) (acknowledging that the boilerplate language in Tax Court opinions might reflect the current "views" of the STJ, not the original findings, and that those original findings might have been "revised"). Rather, that formulaic recitation masks – indeed we find it difficult to avoid any conclusion but that it is designed to mask – a process by which the Tax Court changes findings of fact without any notice to the parties and without leaving a trace in the record. The Tax Court judge apparently discusses such changes (or perhaps does not discuss them at all) and privately "persuades" the trial judge (employed at the will of the Tax Court) to sign a new opinion with completely modified findings. As in this case, only that new opinion is made available to the parties or the courts of appeals.

Before 1983, decisions expressly indicated when the Tax Court judge rejected the trial judge's findings. Opinions would state that "we disagree with the Special Trial Judge,"[5] or that the Tax Court had made "some modifications" to the trial judge's report.[6] But once the Tax Court changed its rule

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[5] See, *e.g.*, *Rosenbaum*, *supra*, n.4, 45 T.C.M. at 827.

[6] See, *e.g.*, *Taylor* v. *Comm'r*, 41 T.C.M. (CCH) 539 (1980).

to deny access to the trial judge's report, the Tax Court never again manifested any such disagreements in public. Judge Cudahy concluded, and the Commissioner does not deny, that the public show of unanimity on every factual finding in every case over two decades signals that the Tax Court, in at least some cases, overturns or modifies STJ original findings of fact through an unreviewable process that leaves no trace in the public record. Pet. App. 74a. In any given case, there is no way to know whether such modification has occurred.

The Tax Court need not hear any witnesses or take any new evidence before issuing its decision and did not do so in this case. The only materials before the Tax Court judge were the trial judge's report and the trial record. If the Tax Court rejects the Special Trial Judge's presumptively correct findings, neither the parties nor the reviewing court have any way to know of that fact. The taxpayer is denied the opportunity to challenge that rejection, either by motion in the Tax Court[7] or on appeal, and the reviewing court is unable properly to evaluate the findings contained in the Tax Court's final decision. Without knowing whether the Tax Court decision rests on findings fundamentally different from those in the report of the judge who tried the case, the court of appeals cannot determine whether the Tax Court has properly followed the requirements of Rule 183. Nor can the court of appeals meaningfully judge on the record as a whole whether the findings of fact in the newly minted Tax Court opinion are clearly erroneous. Absent the Rule 183 report, the court cannot evaluate the Tax Court's decision in the manner prescribed by law. As Judge Cudahy concluded, "I do not believe that the concealment behind that [boilerplate] verbal formula allows this court to conduct meaningful appellate review." Pet. App. 96a-97a. Numerous

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[7] See Tax Ct. R. 161 (motion for reconsideration of findings or opinion); Tax Ct. R. 162 (motion to vacate or revise decision).

commentators similarly have concluded that the Tax Court practice violates due process or other federal law.[8]

3. Tax Court Proceedings in This Case. Burton W. Kanter was one of the leading estate-tax lawyers in the country, a prolific writer on tax planning, and an adjunct professor of law for nearly 15 years at the University of Chicago Law School. Kanter and others sought review in the Tax Court of notices of deficiency that, with interest and penalties, totaled more than $30 million. The notices did not claim fraud, but the Commissioner later amended his answer to allege fraud. All income from the transactions at issue was fully reported by the entities that actually received the money; the dispute was whether the income should have been reported by Kanter personally, as the Commissioner claimed, or by the entities that actually received the monies, as Kanter claimed.

The Chief Judge of the Tax Court assigned the trial to Special Trial Judge Couvillion. That trial before Judge

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[8] See, *e.g.*, Eric Winwood, *The Reclusive Report: The Tax Court Denies Due Process By Not Disclosing Special Trial Judge Reports To Litigants*, 2004 FED. CTS. L. REV. 3; Leandra Lederman, *Transparency and Obfuscation in Tax Court Procedure*, 102 TAX NOTES 1539, 1541 (March 22, 2004) (non-disclosure of the STJ report improperly "shields the [tax] court from accountability"); Gerald A. Kafka & Jonathan Z. Ackerman, *Fact-Finding in the Tax Court: Access to Special Trial Judge Reports*, 91 TAX NOTES 639, 642 (April 23, 2001) ("There seems to be little justification for the Tax Court to shroud its judicial processes from the public and the parties to a greater extent than any other federal court."); Cornish F. Hitchcock, *Public Access to Special Trial Judge Reports*, 2001 TAX NOTES TODAY 199-41 (Oct. 12, 2001) (non-disclosure of STJ report violates common-law and constitutional rights of access to judicial documents). One of these authors is not the only Kafka one can imagine taking an interest in the legal procedure utilized by the Tax Court. *Cf.* F. Kafka, The Trial (1925).

Couvillion consumed five weeks and "generated almost 5,500 pages of transcript, more than 4,600 pages of briefs and thousands of exhibits consuming hundreds of thousands of pages." Pet. App. 3a. Judge Couvillion prepared and filed the required Rule 183 report after taking four years to evaluate the massive record. J.A. 7. His report included findings of fact, critical judgments of credibility, and legal conclusions on the issue of fraud. The Chief Judge then assigned Tax Court Judge Dawson to review the report. Pet. App. 113a-114a.

Judge Dawson had the report under review for fifteen months. He heard no new witnesses and took no new evidence. At the end of that time, Judge Dawson issued the Tax Court's decision that found Kanter liable for tax fraud. *Inv. Research Assocs., Ltd.* v. *Comm'r*, 78 T.C.M. (CCH) 951, 963 (1999).

Two judges of the Tax Court then came forward to Tax Court counsel and informed him that Judge Dawson's decision had completely reversed the central findings of credibility and intent contained in the trial judge's Rule 183 report. That report had found Kanter and others not liable for fraud and not liable even on the underlying issues of personal tax liability.[9] This evidence is uncontradicted and the Commissioner does not contest these factual assertions.

These two Tax Court judges (one a regular Tax Court judge, the other the Chief Special Trial Judge) informed counsel:

> "¶4 * * * [I]n his original report submitted to the Chief Judge pursuant to Rule 183(b), Special Trial Judge Couvillion concluded that payments made by the [taxpayers] were not taxable to the

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[9] See *Declaration of Attorney Randall G. Dick*, filed in *Inv. Res. Assoc.* v. *Comm'r*, Docket No. 43966-85, reprinted at App. 5a-7a.

> individual Petitioners and that the fraud penalty was not applicable.
>
> "¶5 * * * That substantial sections of the opinion were not written by Judge Couvillion, and that those sections containing findings related to the credibility of witnesses and findings related to fraud were wholly contrary to the findings made by Judge Couvillion in his report. The changes to Judge Couvillion's findings relating to credibility and fraud were made by Judge Dawson."

App. 6a. A third judge of the Tax Court confirmed that Judge Dawson "had made an outright rejection of credibility findings made by a Special Trial Judge." *Id.* at ¶7.

Witness credibility was central to this tax fraud case, as it often is in such cases. See, *e.g.*, *Laird* v. *Comm'r*, 68 T.C.M. (CCH) 1991 (1994); *Platshorn* v. *Comm'r*, 64 T.C.M. (CCH) 1457 (1992). The government bears the burden of proving, by clear and convincing evidence, that a taxpayer has acted with intent to defraud the government. See, *e.g.*, *Pittman* v *Comm'r*, 100 F.3d 1308, 1312-13 (7th Cir. 1996). In this case, 60 witnesses testified at the lengthy trial; the trial judge directly questioned 40 of them.

The Tax Court's final opinion rests upon numerous explicit credibility determinations.[10] But the record reflects neither the Special Trial Judge's original findings to the contrary on these matters, nor the Tax Court's reversal of those findings. Nor does it explain or justify that reversal

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[10] See, *e.g.*, 78 T.C.M. at 1060 ("We find Kanter's testimony to be implausible."); *id.* at 1079 ("The testimony of Thomas Lisle, Melinda Ballard, Hart, and Albrecht is not credible."); *Id.* at 1083 ("we find Ballard's testimony vague, evasive, and unreliable"); *id.* at 1104 ("Kanter's self-serving testimony is not persuasive"); *id.* at 1140 ("[T]he witnesses presented on behalf of IRA in this case were obviously biased, and their testimony was not credible.").

(under any standard of review at all). The final decision simply concludes: "Kanter's testimony at trial was implausible, unreliable, and sometimes contradictory. We did not find it credible." *Inv. Research Assocs., Ltd.*, 78 T.C.M. (CCH) at 1085.

In response to three separate motions filed shortly after the Tax Court's decision, the Tax Court refused to have the trial judge's report released or made part of the record. Pet. App. 99a, 104a, 107a. Rather than providing the report that would enable the Article III appellate court independently to review the Tax Court decision for compliance with law, the Tax Court simply professed its own compliance with all legal requirements: "[i]n reviewing the Special Trial Judge's report, Judge Dawson gave due regard to the fact that Special Trial Judge Couvillion evaluated the credibility of witnesses . . . and he treated the findings of fact recommended by the Special Trial Judge as being presumptively correct." Pet. App. 108a.[11]

4. The Seventh Circuit's decision. A divided panel of the court of appeals affirmed. The majority concluded that "the Tax Court's final opinion is the STJ's report" and hence that Petitioners' constitutional claims were "moot" and "immaterial." Pet. App. 7a. This conclusion reflected understandable confusion, caused by the Tax Court's opaque process, which concealed the fact that the Tax Court's opinion is *not* necessarily the trial judge's "report." The

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[11] A subsequent Tax Court order, issued after the declaration was filed that described the two Tax Court judges' disclosure to Tax Court counsel of the reversals of findings contained in the Tax Court's opinion, is more ambiguous about whether Judge Dawson deferred to the findings contained in the original report. See Pet. App. 102a (stating that the Tax Court had adopted the "findings of fact and opinion" of the Special Trial Judge, but not stating that the Tax Court had adopted the findings and opinion contained in the Special Trial Judge's Rule 183 Report).

Commissioner no longer defends the Tax Court opinion on this ground. See *supra* at p.9. The government acknowledges that the Tax Court may have dramatically changed the findings of fact and credibility judgments in the original trial judge report.

Alternatively, the court of appeals held that "even if * * * the phrase 'agrees with and adopts' masks what is in fact a quasi-collaborative judicial deliberation in which an STJ's initial findings are malleable," Pet. App. 7a, neither due process nor applicable federal statutes are violated when the Tax Court changes "malleable" trial-judge findings without the record reflecting or justifying those changes.

The foundation of this conclusion was the court's view that Rule 183 does not constrain at all the reviewing powers of the Tax Court judge. In conflict with the D.C. Circuit's view that the Rule imposes a "clearly erroneous" standard for review by the Tax Court of the Special Trial Judge's findings of fact, the court below concluded that the Tax Court Rules do not "prescribe any particular level of deference due the STJ's report." Pet. App. 8a. Moreover, the court noted that the final decision is signed by both the Tax Court judge and the Special Trial Judge. Thus, although the Special Trial Judge serves at the pleasure of the Tax Court, the court concluded that both judges must have "agree[d]" on whatever secret revisions the Tax Court judge made to the trial judge's original findings. Pet. App. 7a.

Judge Cudahy dissented. In his view, the Tax Court's refusal to disclose the original trial judge's findings of fact made it impossible for the Article III reviewing court properly to review the findings contained in the Tax Court's ultimate decision in violation of due process. Congress specifically required the appellate courts to ensure that Tax Court findings of fact are not clearly erroneous. *Duberstein,* 363 U.S. at 291 n.13. As Judge Cudahy noted, proper

application of that standard requires an appellate court to overturn a finding of fact when,

> although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed. . . . When findings are based on determinations regarding the credibility of witnesses, [clear error review] demands *even greater deference* to the trial court's findings. . . .

Pet. App. 89a-90a (quoting *Anderson* v. *City of Bessemer City, 470* U.S. 564, 573-75 (1985)) (citations omitted).

Yet absent the original trial judge's findings and report, Judge Cudahy concluded, the reviewing court simply cannot perform proper "clearly erroneous" review. The reviewing court, confronting a finding of fact, cannot tell whether that finding is due the "greater deference" owed to actual trial judge findings, or whether that finding is due considerably less deference precisely because it reflects a *rejection* of the original trial judge's findings.

As Judge Cudahy summarized, "If we are to give 'even greater deference' to the findings of a judge who has heard the witness whose credibility is at stake, we must inevitably give less deference to the judge who subsequently reverses those findings." Pet. App. 90a. But without the Special Trial Judge's original findings and report, it is impossible to identify which findings are made by the trial judge and which involve new or modified findings of the Tax Court judge. Judge Cudahy concluded that this system made it impossible for him to perform his legal duty to provide proper appellate review. Pet. App. 94a. He reasoned that this was so whether or not the Tax Court owed any particular level of deference, or no deference at all, to the trial judge's findings. Judge Cudahy therefore concluded that the Tax Court's practice, which regularly and systematically frustrated proper appellate review, violated due process. He also found that

the relevant federal statutes should be construed to require transparency in Tax Court proceedings and to prohibit the Tax Court's practice of non-disclosure. Pet. App. 83a.

SUMMARY OF ARGUMENT

I. Secret trial judge reports violate due process and the appellate review statute, 26 U.S.C. §7482(a), by preventing proper appellate review in the courts of appeals. Tax Court Rule 183(c) requires the Tax Court to give deference to the trial judge's findings of fact, to presume those findings correct, and to afford due regard to the circumstance that the trial judge had an opportunity to observe witnesses and judge credibility. That Rule gives the trial judge's findings legally operative effect in the Tax Court's final decision. The denial of access to findings of fact that, by law, carry legal weight in the final decision of a formal adjudication violates due process. The Tax Court's practice precludes the Article III reviewing courts from determining whether the Tax Court gave proper legal deference to the trial judge's findings and properly treated them as presumptively correct.

That the Tax Court's practice violates due process is confirmed by the longstanding historical and contemporary practice of every other federal judicial or administrative institution, all of which view disclosure of the original factfinder's or hearing officer's report to be integral to fundamentally fair adjudicative process. Application of the balancing test of *Mathews* v. *Eldridge*, 424 U.S. 319, 335 (1976) also confirms that the Tax Court's practice violates due process. Disclosure of the trial judge's findings can only enhance accurate decisionmaking and entails virtually no cost, given that these findings must already be prepared and filed with the Tax Court. The proper outcome of the *Mathews* balance is reflected in the consensus of both Congress and other federal rulemakers that such findings must be disclosed in all other federal judicial and administrative adjudications.

II. Rule 183 permits the Tax Court to overturn a trial judge's findings only if "clearly erroneous." The plain language and history of the Rule make this clear. See *Stone* v. *Comm'r*, 865 F.2d 342, 345 (D.C. Cir. 1989). The government's post-hoc litigation position, that the Rule requires no deference at all from the Tax Court to its trial judges, is insupportable.

III. Even if the Special Trial Judge's report were considered of no formal legal relevance to the Tax Court's final decision – as the government argues - due process would still require the report's release. First, failure to disclose the trial judge's original findings precludes the court of appeals from properly applying the clear error standard of review, as this Court has defined that standard. See *Anderson* v. *Bessemer City*, 470 U.S. 564 (1980).

Second, if the Tax Court judge were somehow viewed as an original factfinder, Petitioners would be entitled as a matter of due process to see all the information in front of that judge when he makes his findings of fact and to address before that judge the factual issues on the basis of which his original factfinding determinations are made.

IV. Secret Special Trial Judge reports also violate the transparency and disclosure requirements in the statutes that govern Tax Court proceedings. From the inception of the modern income tax, Congress has imposed special requirements of transparency and openness for every phase of Tax Court proceedings. 26 U.S.C. §7461(a); §7459(b). Section 7461(a) requires that all "reports of the Tax Court and all evidence received by the Tax Court shall be public records." The Special Trial Judge's report is included in those terms. And if there were any doubt, the common-law right of access to judicial records would counsel in favor of interpreting these statutes to include the Special Trial Judge's Report.

V. Finally, this Court should exercise its supervisory power to require that the courts of appeals review Tax Court decisions on the same basis as that used for all other federal courts and, indeed, all agencies by requiring that the record include the report of the trial judge who presided at trial, heard the witnesses, and made recommended, legally operative findings. The Tax Court's practice of secrecy is a stark example of a "depart[ure] from the accepted and usual course of judicial proceedings" that warrants this Court's intervention. See SUP. CT. R. 10(a).

ARGUMENT

I. DUE PROCESS AND THE APPELLATE REVIEW STATUTE REQUIRE DISCLOSURE OF A TRIAL JUDGE'S FINDINGS OF FACT THAT HAVE LEGALLY OPERATIVE WEIGHT IN A COURT'S FINAL DECISION.

The government has some discretion, within constitutional constraints, to choose how to construct institutions of formal adjudication. Once it creates judicial (or administrative) institutions with certain structures, however, due process requirements attach. The Tax Court need not use Special Trial Judges, but once it does, due process requires that it disclose the presumptively correct findings those judges have made.

Tax Court Rule 183 (c) provides that: "Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Tax Ct. R.183(c). That rule embodies and reflects traditional understandings concerning how to structure fundamentally fair and accurate adjudicative processes. The Courts of Appeals are, of course, bound to review decisions of the Tax Court for compliance with law, including compliance with Rule 183. See 26 U.S.C. §7453; see, *e.g.*, *Service* v. *Dulles*, 354 U.S. 363, 388

(1957) (agency legally required to comply with its own regulations).

Rule 183(c) by its plain terms commands deference by the Tax Court to the Special Trial Judge's original findings of fact. As long as that Rule requires any level of deference at all from the Tax Court, the findings of the trial judge are legally required to have weight in the Tax Court's ultimate decision. Yet the Tax Court's practice makes it literally impossible for a reviewing court to determine whether the Tax Court has complied with Rule 183(c) by giving those findings the required deference. Without seeing the report filed by the judge who tried the case, a court of appeals cannot assess whether the Tax Court has properly construed and applied its legal obligations to "presum[e] correct" the STJ's findings and to give "[d]ue regard" to the STJ's opportunity to evaluate the credibility of witnesses.

A. A Reviewing Court Must Have Access To The Information Necessary To Evaluate The Decision Before It.

Due process requires that a court reviewing a legal determination must have before it the information necessary to determine and evaluate the basis upon which a lower court has made its decision. Long ago, this Court recognized the basic principle that due process is denied, even in administrative decisions, when an adjudicator bases its decision upon facts that it "never . . . disclosed." *Ohio Bell Tel.* v. *Pub. Utilities Comm'n of Ohio*, 301 U.S. 292, 300 (1937). As Justice Cardozo concluded, "From the standpoint of due process – the protection of the individual against arbitrary action – a deeper vice is this, that even now we do not know the particular or evidential facts . . . on which [the state regulatory Commission] rested its conclusion. Not only are the facts unknown; there is no way to find them out." *Id.* at 302. This incomplete record not only made the Commission's proceedings a violation of due process, but

further violated due process by rendering the appeal "an empty for[m]," denying the "opportunity in connection with a judicial review of the decision" to properly challenge the basis for the Commission's decision. *Ibid.*

The Tax Court's procedure of keeping secret the legally operative findings of fact made by the trial judge arbitrarily denies Petitioners the adjudication to which they are legally entitled before the appellate court. Due process requires that the parties and courts have access to any initial findings of fact that have legally operative effect in a formal adjudication. This is as true of the appellate courts as it is of the trial courts; where an appeal is granted, it must be a meaningful one. See *Evitts* v. *Lucey*, 469 U.S. 387, 393 (1985) (requirements of due process apply on appeal).

The proceedings before the courts of appeals – which are, absent certiorari review in this Court, the only Article III tribunal that hears the cases that arise in the Tax Court – would violate due process were those courts to render decisions after being presented with only random portions of the record below. Similarly, if appeals were based on biased records – if the Tax Court only included in the record findings or evidence that favored the winning party – due process would be violated. Yet these scenarios are much like the context here: the Tax Court suppresses from the record the original findings of the trial judge that are contrary to those of the Tax Court itself. Appeals are being decided on the basis of partial records – partial both in the sense that that the record is incomplete and that the record is purged of all findings contrary to those of the Tax Court judge.

A fair adjudication in the court of appeals cannot lawfully be denied by a government process that arbitrarily eliminates those rights. Due process requires that a court adjudicating a case be permitted to do so on the merits. See *e.g.*, *Logan* v. *Zimmerman Brush Co.*, 455 U.S. 422, 429, 433-34 (1982) (determination of a cause without "the opportunity to present

[the] case and have its merits fairly judged" violates due process); *West Ohio Gas* v. *Pub. Utilities Comm'n*, 294 U.S. 63, 68-69 (1935) ("To make [judicial] review adequate the record must exhibit in some way the facts relied upon by the court. . . If that were not so, a complainant would be helpless. . . . A hearing is not judicial, at least in any adequate sense, unless the evidence can be known.").

Absent the trial judge's original findings, it is impossible for the Article III courts to evaluate whether the Tax Court indeed presumed correct the trial judge's findings. Neither in the courts of appeals, nor in the Tax Court through a motion for reconsideration or to vacate, can a litigant protect its right to have the trial judge's findings properly respected. A Tax Court judge could overturn those findings for any reason at all – indeed, for personal, political, or ideological reasons – with no federal court review possible.[12] As a categorical rule, due process requires that findings of fact that, by law, carry legal weight in the ultimate adjudicative decision under review must be disclosed. *Cf. Crawford* v. *Washington*, 124 S. Ct. 1354, 1373 (2004) (constitutional guarantees of proper legal process must be protected through categorical rules to withstand inevitable pressures in controversial cases).

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[12] In this case, the Fifth Circuit on a petition for mandamus recently issued a strongly worded ruling rebuking the Tax Court for attempting to continue to impose penalties on one of the taxpayers even after the Fifth Circuit's reversal of the Tax Court's judgment of fraud against him. See *In re Estate of Lisle*, No. 03-61075 (5th Cir. Jan. 7, 2004), reprinted at App.1a (cautioning Tax Court not to exceed scope of the Fifth Circuit's remand after Judge Dawson asserted that he would use the remand to impose new penalties for negligence and substantial underpayment); see also *Lisle* v. *Commissioner*, Docket No. 21555-91 (T.C. Nov. 19, 2003) (Judge Dawson's underlying order), reprinted at App. 3a.

B. Uniform Historical And Contemporary Practice Make Clear That Disclosure Of A Trial Judge's Findings Of Fact Is Essential To Fair, Formal Adjudication.

Disclosure of the findings of a trial judge, hearing officer, or analogous initial factfinder is indeed such a fundamental premise of proper judicial (and even administrative) process that Petitioners have been unable to find *any* area in modern federal law where such disclosure is not routine. Whether the initial factfinder is a special master, a magistrate, a bankruptcy judge, or an administrative law judge – all of whom may have lesser responsibilities than a trial judge who presides over a 28-day trial involving constitutionally protected liberty and property interests – Congress or the relevant federal rules require routine disclosure of initial findings of fact.

The report of a magistrate judge is served on the parties and becomes part of the record. 28 U.S.C. § 636(b)(1)(C). A special master's report must be filed with the District Court and served on the parties (unless the District Court directs otherwise). See FED. R. CIV. P. 53(f); 53 (g)(1),(2). The initial findings of a bankruptcy judge are part of the record. FED. R. BANKR. P. 8013. Even in the administrative agency area, regardless of the nature of the private interest affected, the report of an initial hearing officer is a critical and routine part of the record. The Administrative Procedure Act (APA), 5 U.S.C. § 557(c)(3), requires that "[a]ll decisions, including initial, recommended, and tentative decisions, are a part of the record and shall include a statement of (A) findings and conclusions, and the reasons or basis therefore, on all the material issues of fact, law, or discretion presented on the record; . . .." See also 5 U.S.C. §706 ("the court shall review the whole record or those parts of it cited by a party...").[13]

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[13] The framers of the APA considered these to be critical requirements of properly and fairly structured adjudicative

As the government itself acknowledged below, "in every milieu except that of the Tax Court, the document containing the findings or recommendations of the official conducting the trial are available to a court reviewing the operative decision." Pet. App. 71a (Cudahy, J., dissenting). That is so even when, unlike here, constitutionally protected liberty and property interests are not at stake. It is also so even when, also unlike here, those original findings do not have legal weight in the final decision at issue. See *infra* pp. 34-39.

This consistent, longstanding practice of all federal judicial and administrative institutions confirms that an integral aspect of fair, formal adjudication is that all findings of fact, particularly those that carry legal weight in the final adjudicative decision, must be disclosed. Indeed, this historical practice is so consistent and deeply embedded that, even standing alone, that practice itself would suffice to establish a due process violation. *Cf. Burnham* v. *Superior Court*, 495 U.S. 604, 609 (1990) (plurality opinion of Scalia, J., joined by Rehnquist, C.J., and Kennedy and White, JJ.) ("due process 'mean[s] a course of legal proceedings according to those rules and principles which have been established in our systems of jurisprudence for the protection and enforcement of private rights'") (quoting *Pennoyer* v. *Neff*, 95 U.S. 714, 733 (1978)).

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proceedings, particularly "on matters which the hearing commissioner, having heard the evidence and seen the witnesses, is best qualified to decide . . . ." Report of the Committee on Administrative Procedure, Administrative Procedure in Government Agencies 51 (1941). See also 2 Pierce, ADMINISTRATIVE LAW TREATISE § 11.6 at 822 (2002) (the "initial decision of the ALJ" must form part of that record in any "formal adjudication").

C. Disclosure Is Also Required By The *Mathews* v. *Eldridge* Balancing Test.

Application of the *Mathews* v. *Eldridge* balancing test generates the same constitutional result. *Mathews* v. *Eldridge*, 424 U.S. 319, 335 (1976). See also *Hamdi* v. *Rumsfeld*, 124 S. Ct. 2633, 2646-2650 (2004) (controlling plurality opinion of O'Connor, J.) (applying *Mathews*).

Mathews requires the Court to weigh (1) the private interests at stake; (2) the effect on decisionmaking accuracy of the procedure sought; and (3) the administrative or other burdens of that procedure. 424 U.S. at 335. Petitioners are not seeking a novel procedure that this Court must assess on a blank slate: Congress and the federal courts have already weighed these interests and concluded in every other context that accurate and fair adjudication requires disclosure of similar initial findings.

Indeed, it is not clear that Petitioners, in seeking disclosure, are even seeking the kind of additional procedure to which *Mathews* was addressed. The trial judge must already prepare and submit to the Tax Court the report at issue. Petitioners are seeking *disclosure* of a report and findings that must already be prepared, not an additional procedural step, such as a requirement that such a report be prepared. As Judge Cudahy found, "[t]he Tax Court has not denied that a document containing the original findings of the STJ exists, yet it refuses to include this document in the record on appeal." Pet. App. 71a.

More formally, with respect to prong (1) of *Mathews*, the private interests at stake, both constitutionally protected property and liberty interests are implicated when tax fraud is alleged. Government action that seriously damages an individual's reputation in the course of taking away property implicates both liberty and property interests. See, *e.g.*, *Wisconsin* v. *Constantineau*, 400 U.S. 433, 437 (1971); *Owen* v. *City of Independence*, 445 U.S. 622, 682 n.13

(1980). A civil tax fraud action is a quasi-criminal proceeding; only a criminal trial would involve weightier interests. See, *e.g.*, *Addington* v. *Texas*, 441 U.S. 418, 424 (1979) (noting that "[t]he interests at stake in [civil fraud] cases are deemed to be more substantial than mere loss of money" because of the "risk to the defendant of having his reputation tarnished erroneously"); *Guenther* v. *Comm'r*, 889 F.2d 882, 884 n.2 (9th Cir. 1989) (precedent from criminal cases relevant to due process in tax fraud proceedings before Tax Court, because "civil fraud is such a serious charge").

With respect to prong (2), review based on the whole record that was before the tribunal whose decision is under review has long been viewed as essential to accurate decisionmaking in formal adjudications. If Rule 183 requires the Tax Court to defer at all to the trial judge's original findings, it is metaphysically impossible for the courts of appeals to engage in accurate review without those findings. But even were the Rule to require no formal deference, accurate review would still require review on the whole record. Courts of appeals commonly reverse agency decisions under the substantial evidence test, for example, when an agency has reversed the findings of its administrative law judges and failed to provide a sound explanation for doing so, even when the agency itself has *de novo* factfinding power. See *infra* note 15. This pattern confirms the principle, reflected in central commitments of statutes like the APA, that accurate decisionmaking requires courts to review adjudications on the basis of the whole record.

Finally, with respect to prong (3), disclosure implicates virtually no administrative burden at all. The only "burden" is that disclosure would enable the courts of appeal to review the Tax Court's decisions on the basis of the whole record. But proper accountability to appellate review cannot count as a burden, even a minimal one, for due process analysis. It

can only be a benefit. At no time has the government, either through a Tax Court opinion or in post-hoc litigation, advanced even a plausible governmental interest in maintaining this unique, secretive process. There is no cost at all that due process can recognize to the Tax Court of disclosing a report that must already be prepared and filed. Disclosure of initial, recommended, and other findings of fact is required in adjudications that do not implicate constitutionally protected interests at all. The *Mathews* balance requires at least as much here.

D. The Appellate Review Statute Also Requires Disclosure.

Even apart from the Constitution, the failure to disclose the Special Trial Judge's Report violates the appellate review statute. The courts of appeals have a statutory duty to review Tax Court's decisions "in the same manner and to the same extent" as they review district court decisions in non-jury civil cases. 26 U.S.C. § 7482. The failure to disclose the Special Trial Judge's report makes this impossible.

As described above, reports and recommendations of special masters, magistrate judges, and bankruptcy judges are publicly available components of the record when a case is appealed from the district court to the court of appeals. These are necessary in order for the court of appeals to engage in meaningful appellate review of the district courts' decisions.

To evaluate the Tax Court's decision for compliance with Rule 183(c) and to properly employ the legally controlling clearly erroneous standard of review, the court of appeals similarly requires access to the report and findings of the Special Trial Judge. The failure to provide the courts of appeals with that report renders impossible review in the same manner and to the same extent as review of decisions of the district courts. That is a violation of 26 U.S.C. §7482. *Cf. Sumner* v. *Mata*, 449 U.S. 539, 549 (1981) (holding that

federal courts would improperly frustrate intent of habeas corpus statute by issuing boilerplate statements that they had considered the state record as a whole and concluded that the state appellate court's factual determinations were not fairly supported by the record as a whole). For further argument that the Tax Court practice violates 26 U.S.C. § 7482, see Brief *Amica Curiae* of Professor Leandra Lederman in Support of Petitioners.

The Commissioner has never responded to the argument that, if the Rule requires any deference at all, due process must require the original findings to be part of the record. Instead, the government asserts that the Rule requires no deference at all. As the next Sections show, that interpretation defies the text and history of the Rule, and even were that reading correct, due process would still require the Tax Court to include the report in the record.

II. RULE 183(C) ESTABLISHES A CLEARLY ERRONEOUS STANDARD OF REVIEW.

Tax Court Rule 183 specifies that the reviewing Tax Court judge must give "due regard" to the trial judge's "opportunity to evaluate the credibility of witnesses" and that the "findings of fact recommended by the special trial judge shall be presumed to be correct." Those familiar terms permit the Tax Court to reject the Special Trial Judge's factual findings only if clearly erroneous. That is the conclusion the D.C. Circuit reached in a detailed analysis authored by Judge Williams fifteen years ago in *Stone* v. *Comm'r*, 865 F.2d 342, 345 (D.C. Cir. 1989). See also *Landry* v. *FDIC*, 204 F.3d 1125, 1133 (D.C. Cir. 2000) (relying on *Stone*). Yet the government contends that Rule 183(c) does not require any level of deference to the findings of the trial judge who presided over this five-week trial. Opp. at 15.

The government's position disregards the Rule's text and ignores its history. Even if the Rule required no deference at

all to trial judge findings, suppressing those findings from the record would still violate due process. See *infra* at pp. 34-42. But the Rule does require the Tax Court to perform "clear error" review.

A. The Rule By Its Plain Meaning Establishes A Clearly Erroneous Standard of Review.

The plain meaning of a rule that requires trial judge findings to be "presumed . . . correct" and to be given "due regard" is that the Tax Court judge must defer to those findings. In asserting that the rule requires no particular level of deference, the government would read this presumption out of the rule.

Moreover, the terms "presumed to be correct" and "due regard" are well known to American law. These phrases mean that findings shall be reviewed under a "clearly erroneous" standard. As *Stone* concluded, these terms reflect "language with a reasonably well-established meaning" whose "natural reading" is review only for clear error. 865 F. 2d at 347. Indeed, this Court has equated "the presumption of correctness that attaches to factual findings" with the "clearly erroneous" standard of review. See, *e.g.*, *Bose Corp.* v. *Consumers Union*, 466 U.S. 485, 500 (1984). The habeas corpus statute expressly states that state court findings of fact "shall be presumed to be correct" by the federal courts, and that statute, too, has been held by this Court to permit rejection of state court factual determinations only after giving great deference to the state court's findings. See *Sumner* v. *Mata*, 449 U.S. 539 (1981) (so holding and reversing on the ground that the opinion of the court of appeals had not given any indication whether the correct level of deference had been paid).

The use of a "presumption" with respect to a "finding" imposes a "standard of review." See *Concrete Pipe & Prods. of Cal., Inc. v. Constr. Laborers Pension Trust for S. Cal.*, 508 U.S. 602, 623-625 and n.15 (1993). When a higher-level

body instead is to have *de novo* power over factfinding, it is easy enough to specify that. See, *e.g.*, Fed. R. Civ. Pro. 53 (g)(3) (District Court "must decide *de novo* all objections to findings of fact made or recommended by a master . . ."). We have found no federal statute or rule where the phrases "due regard" and "presumed to be correct" are associated with *de novo* review or license a reviewing judge or court to give "no deference" to the hearing officer's factual findings. As Judge Williams concluded in *Stone*: "If a simple 'preponderance' of the evidence – half plus a little bit – suffices to overturn the factual findings of a Special Trial Judge, then it is difficult to see what value or force attaches to the presumptive correctness of that judge's factual determinations, much less the 'due regard' owed 'to the circumstance that the [Special Trial Judge] had the opportunity to evaluate the credibility of witnesses.'" *Stone*, at 347.

B. The History and Context of Rule 183 Confirm This Plain Meaning.

The history of the adoption of Rule 183 supports the conclusion that the Rule means what it says. The language now contained in Rule 183(c) was originally taken from Rule 147(b) of the former Court of Claims.[14] When the Tax Court

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[14] Rule 147(b) of the former Court of Claims read:

> (b) **Trial Judge's Report**. The court may adopt the trial judge's report, including conclusions of fact and law, or may modify it, or reject it in whole or in part, or direct the trial judge to receive further evidence, or refer the case back to him with instructions. *Due regard shall be given to the circumstance that the trial judge had the opportunity to evaluate the credibility of the witnesses; and the findings of fact made by the trial judge shall be presumed to be correct.*

adopted the language now codified in Rule 183(c) (which at the time referred to "commissioners") the Tax Court clarified in an explanatory note that it was drawing directly on the Court of Claims rule:

> [T]he commissioner's findings of fact * * * are accorded special weight insofar as those findings are determined by the opportunity to hear and observe the witnesses. In this regard, see Court of Claims Rule 147(b). * * * This rule is intended to make the use of commissioners more effective, and to provide procedures more comparable to those which obtain in the Court of Claims.

Tax Ct. R.182(d), *26 U.S.C. App. (1976)*, 60 T.C. 1150.

When the Tax Court adopted this rule in 1973, it was clear that the Court of Claims rule, with its "due regard"/"presumed to be correct" language, embodied a clearly erroneous standard of review. See *Elmers* v. *United States*, 172 Ct. Cl. 226, 232 (1965) (objector bears "burden of showing that the commissioner's finding is clearly erroneous"); see also Court of Claims Committee of the Bar Ass'n of D.C., MANUAL FOR PRACTICE IN THE UNITED STATES COURT OF CLAIMS 7 (1976) ("once a trial judge has rendered his fact findings, the court accords great weight thereto and will not lightly overturn such determinations by its trial judges."); *J.G. Watts Constr. Co.* v. *United States*, 355 F.2d 573, 579 (Ct. Cl. 1966).

Thus, when the Tax Court adopted Rule 182 and then renumbered it as Rule 183, it borrowed a highly deferential standard of review for STJ findings. That is what the D.C. Circuit held in *Stone* v. *Comm'r*, 865 F.2d 342 (D.C. Cir. 1989). The *Stone* court examined "the natural reading" of

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Court of Claims Rule 147(b), 28 U.S.C. App. (1976) (emphasis added), *rendered nugatory*, Claims Court Rules Foreword, 28 U.S.C. App. (1982).

Rule 182's text, the legislative history of the Rule, and the use of similar language in other areas of federal law. It concluded that, by adopting the "due regard"/"presumed to be correct" formulation, the drafters "sought to establish the relatively high level of deference that the phrase 'clearly erroneous' entails." 865 F.2d at 344. The court rejected the argument that the Rule requires no deference at all or only a "mild presumption in favor." *Id.* As *Stone* concluded, the "natural reading" of the Rule imposes a "clearly erroneous standard." *Id.*

Since *Stone,* commentators have understood Rule 183 to continue to establish a "clearly erroneous" standard. 35 AM. JUR. 2d *Fed. Tax Enforcement* § 905 (2002) ("The Tax Court is required to review a special trial judge's factual findings according to the clearly erroneous standard."); 20A FEDERAL PROCEDURE, L. ED., INTERNAL REVENUE § 48:1274 (2000) (same).

The government does not dispute that *Stone* was correct when decided. The government concedes that, at least until 1983, the Tax Court rule did embody a "clearly erroneous" standard. But the government suggests that the role of the Tax Court and the STJ dramatically changed in 1983 when the Tax Court amended the rule that *Stone* had interpreted. See Opp. at 16 (arguing that *Stone* was decided under "the prior rules of the Tax Court"). According to the government, the 1983 amendment transformed the relationship that had existed since 1944 between the Tax Court and its Special Trial Judges (or commissioners). The government's litigation position is that the 1983 amendments turned Tax Court judges into original factfinders and diminished the role of the Special Trial Judge into something akin to a staff attorney. See Opp. 16-17.

Yet the 1983 Rule change did only one thing: it eliminated, without explanation, the sentence in the Rule that required routine disclosure of the STJ's reports. Both before

and after the 1983 amendments, the relevant Tax Court rule has provided that "Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Elimination of the rule mandating publication of the STJ's Report no more changes the role of the Tax Court in reviewing such a report than ending publication of Courts of Appeals' decisions would change this Court's nature as a reviewing court.

And indeed, in *Freytag*, this Court already discussed and rejected the government's argument that a Special Trial Judge acting as here under 26 U.S.C. § 7443A(b)(4) serves "only as an aide to the Tax Court judge responsible for deciding the case." 501 U.S. at 880. Special Trial Judges "exercise significant discretion" when they "take testimony . . . [and] conduct trials," even where they are not authorized to make the final decision of the Tax Court – indeed, these actions and decisions have sufficient legal weight that they constitute an exercise of the judicial power of the United States. 501 U.S. at 882.

The Rule by its terms continues to require the Tax Court to "presume correct" STJ findings. The Tax Court did not, in any contemporaneous publication, interpretive guideline, or any other statement of policy publicly announce then – nor has it at any time since 1983 through today – that the new Rule 183 had fundamentally altered the role of the Tax Court and of its trial judges. The government's position that eliminating *disclosure* changed the *substantive standard of Tax Court review,* overturning the "clearly erroneous" standard recognized in *Stone,* is a post-hoc litigation position. If nothing else, *Stone* put the Tax Court on notice that the court of appeals, in a carefully considered opinion, read the Rule to establish a "clearly erroneous" standard. Yet the Tax Court has not changed the rule since *Stone.* For all these reasons, "due regard" and "shall be presumed to be correct"

in Rule 183 continue to establish a "clearly erroneous" standard of review.

III. EVEN IF RULE 183 REQUIRED NO DEFERENCE AT ALL, DUE PROCESS WOULD STILL REQUIRE RELEASE OF THE SPECIAL TRIAL JUDGE'S REPORT.

Even were the government correct that Rule 183 permits the Tax Court to give no deference at all to the findings of trial judges, due process would still require disclosure of the trial judge's Rule 183 report.

A. Nondisclosure Violates Due Process on Appeal.

First, due process on appeal is violated if the record fails to include the trial judge's report. The courts of appeals are legally required to review for "clear error" the findings of fact in Tax Court decisions. 26 U.S.C. §7482(a); *Duberstein, supra.* That includes findings of fraudulent intent. See, *e.g.*, *Pittman* v. *Comm'r*, 100 F.3d 1308, 1312-13 (7th Cir. 1996).

But the very concept of "clearly erroneous" review *requires* that the findings of an initial trial judge or factfinder be part of that review process. That is so whether or not the tribunal whose ultimate decision is under review is required by its own rules to defer to those findings; the reviewing courts must themselves have access to those findings to perform proper "clear error" review of the facts contained in the final decision under review.

This Court has explained many times that the findings of the original trier of fact are critical to engaging in proper appellate review for "clear error." See, *e.g.*, *Anderson,* 470 U.S. at 564 ("When findings are based on determinations regarding the credibility of witnesses, [the clearly erroneous standard] demands even greater deference to the trial court's findings.") (citations omitted); *United States* v. *United States Gypsum Co.* 333 US 364, 395 (1948).

This is the essential point Judge Cudahy recognized in dissenting below: "it is integral to the standard of clear error review that there be deference to the credibility findings of the official who has actually heard the witnesses." Pet. App. 90a. "If we are to give 'even greater deference' to the findings of a judge who has heard the witness whose credibility is at stake, we must inevitably give less deference to the judge who subsequently reverses those findings." *Id.*

This same principle is a foundational one even in contexts, such as judicial review of agency decisions, that do not involve a formal trial before a judicial institution such as the Tax Court. In a landmark decision, this Court long ago recognized the importance of the initial report of a hearing examiner to accurate appellate adjudication of an agency's final decision. *Universal Camera Corp.* v. *NLRB*, 340 U.S. 474, 496 (1951). As Justice Frankfurter wrote, "evidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion . . . The significance of [the presiding judge's or examiner's] report, of course, depends largely on the importance of credibility in the particular case." The Court so held whether or not the Board was itself required, under its own rules, to give any particular level of deference to the hearing officer.[15]

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[15] Applying substantial evidence review even in the merely administrative context, lower courts regularly overturn agency decisions when they conflict with findings of an initial hearing officer and the agency fails adequately to explain or justify its rejection of those original findings. In the Board of Immigration Appeals context, for example, see *Mayo* v. *Ashcroft*, 317 F.3d 867, 871 (8th Cir. 2002) (BIA cannot reverse an Immigration Judge's credibility findings without a "legitimate articulable basis"); *Abdulai* v. *Ashcroft*, 239 F.3d 542, 555 (3d Cir. 2001) (reversing and remanding "[b]ecause the BIA's failure of explanation [for its

This is not a technical principle of administrative law; it states a general principle that accurate appellate review *requires* review on the whole record when tribunals divide factfinding between one who takes evidence and hears witnesses and one who renders ultimate decision – even in mundane cases. The reviewing court must have access to the original findings of fact, otherwise it cannot properly evaluate (under either the "clear error" or the "substantial evidence" standard) the factual foundation for a tribunal's ultimate decision. This is an essential attribute of accurate and fair adjudication – all the more so in formal adjudications, such as this case, where constitutionally protected individual interests are at stake.

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reversal of the Immigration Judge's favorable credibility finding] makes it impossible for us to review its rationale"); *Diallo* v. *INS*, 232 F.3d 279, 288-90 (2d Cir. 2000) (same). The lower courts uniformly impose these requirements notwithstanding that the decision under review in an immigration case is that of the BIA, not that of the Immigration Judge. See, *e.g.*, *Abdulai*, 239 F.3d at 554 (so holding).

In the context of social-security appeals, see *Bauzo* v. *Bowen*, 803 F.2d 917 (7th Cir. 1986) (requiring explicit justification for Social Security Appeals Council's reversal of credibility determinations made by ALJ); *Parker* v. *Bowen*, 788 F.2d 1512 (11th Cir. 1986) (same); *Lopez-Cardona* v. *Sec. of Health and Hum. Serv.*, 747 F.2d 1081 (1st Cir. 1984) (same); *Parris* v. *Heckler*, 733 F.2d 324 (4th Cir. 1984) (same); *Beavers* v. *Sec. of Health, Ed., & Welfare*, 577 F.2d 383 (6th Cir. 1978) (same). In the context of appeals from decisions of the Merit Systems Protection Board, see *Haebe* v. *Department of Justice*, 288 F.3d 1288, 1301-02 (Fed. Cir. 2002) (so holding, and explaining that "[o]ur review is to determine whether the MPSB had substantial evidence to [support its final decision], but in evaluating substantial evidence we review whether the MPSB properly applied the demeanor-based deference requirement [established by the court's precedents]").

The facts in dispute here are not routine matters of historical or documentary record. They involve judgments of intent and credibility. Nor was this some quick, informal hearing before an administrative officer. This was a five-week trial before a Special Trial Judge in a court of law. Trial judge findings involving credibility always demand "special deference," even more when "trial judges have lived with the controversy for weeks or months instead of just a few hours." *Bose*, 466 U.S. at 516. As Judge Cudahy observed,

> the present case was inordinately long and complicated, and the resolution of issues required the synthesis of multiple witnesses' testimony that was separated by days or even weeks (and by hundreds or thousands of pages in the transcript). Whatever advantage is to be gained by a first-hand observation of witnesses is multiplied exponentially when the trial is so long and the transcript so voluminous. The detailed interconnection of the credibility of different witnesses on different factual issues makes the accumulated impressions of the presiding officer irreplaceable.

Pet App. 93a. The Tax Court's final opinion contains numerous credibility determinations.[16] Tax Court cases tried to Special Trial Judges often involve such credibility determinations.[17] As Judge Cudahy further explained: "I can think of no single item of more significance in evaluating a

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[16] See *supra* note 10.

[17] See, *e.g.*, *Williams* v. *Comm'r*, 86 T.C.M. (CCH) 104 (2003); *Durham Farms #1* v. *Comm'r*, 79 T.C.M. (CCH) 2009 (2000); *Merino* v. *Comm'r*, 74 T.C.M. (CCH) 370 (1997).

Tax Court's decision on fraud than the unfiltered findings of the STJ who stood watch over the trial." *Ibid.* [18]

The trial judge or initial factfinder plays a critical and unique role in formal adjudication, particularly where credibility judgments are involved. The trial judge's recommended findings frequently provide the ultimate decision-maker, as in the Tax Court, with the only means through which it can consider the credibility of trial witnesses. See *United States* v. *Raddatz*, 447 U.S. 667, 681 n. 7 (1980) ("we assume it is unlikely that a district judge would reject a magistrate's proposed findings on credibility when those findings are dispositive and substitute the judge's own appraisal; to do so without seeing and hearing the witness or witnesses whose credibility is in question could well give rise to serious questions which we do not reach"). Due process requires that this unique role and function of the trier of fact be properly respected. That is particularly so here, where the Tax Court itself heard no witnesses and took no new evidence.

The point is not that the Tax Court must hear the witnesses before reversing the Special Trial Judge's findings. The point is that the record fails to reflect whether the Tax Court modified or reversed its trial judge's findings and, if so, on what basis. The Tax Court must let the parties and the

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[18] The Tax Court procedure independently violates Article III of the Constitution. That provision vests in the Courts of Appeals the "judicial power" of the United States. In denying the possibility for meaningful adjudication of the questions of whether there is clear error in the Tax Court's findings of fact and whether that court has complied with the command of Rule 183, the refusal of access to the findings of the judge who tried this case violates Article III. The procedure used by the Tax Court under which the Report is not available to the Courts of Appeals "remove[s] '"the essential attributes of the judicial power,"' from th[ose] Article III tribunal[s]." *Thomas* v. *Arn*, 474 U.S. 140, 154 (1985) (citations omitted).

reviewing courts know whether its findings are based on credibility judgments made by the trial judge, who heard the witnesses and tried the case, or by a subsequent decisionmaker, who did not. Even if the Tax Court owes no deference to the Special Trial Judge's findings, the Tax Court's practice still precludes the court of appeals from performing proper clear error review, which requires review of a record that includes the trial judge's findings.

B. Nondisclosure Also Violates Due Process Before The Tax Court.

Second, even if the government were correct and Rule 183 required no deference to the trial judge's findings, the Tax Court's practice of keeping secret the report of the judge who tried the case would violate the parties' due process rights before the Tax Court.

Regardless of the legal weight Special Trial Judge reports carry, they contain critical evidence – surely the most critical evidence – considered by the Tax Court in rendering its decision. On this point there is no disagreement. See Opp. 15-16. Indeed, the Tax Court heard no witnesses and took no evidence; the *only* materials and evidence before it were the trial judge's report and the trial record. The Tax Court's decision could not have been based on anything else.

This Court long ago made clear that judicial decisions must be based upon a record that is available to the parties. Judicial actors must disclose the documentary and other information upon which they rely in making their decision. Knowledge of the basis upon which one's case is decided is an essential attribute of the adjudication that due process requires. *West Ohio Gas Co.* v. *Public Utilities Comm'n of Ohio*, 294 U.S. 63 (1935) (per Cardozo, J.) (finding a violation of due process where the basis of a public utility commission's decision could not be known to the parties or the reviewing court because "[a] hearing is not judicial, at least in any adequate sense, unless the evidence can be

known."); *see also, e.g.*, *Morrissey* v. *Brewer*, 408 U.S. 471 (1972) (even in the parole context, due process requires a "written statement by the factfinders as to the evidence relied on and reasons for revoking parole"). Indeed, litigants are entitled to an opportunity to supplement, comment on, or explain any materials on which a court bases its decision. See, *e.g.*, *Ohio Bell Tel. Co.* v. *Public Utilities Comm'n of Ohio*, 301 U.S. 292, 302-303 (1937); *Morgan* v. *United States*, 304 U.S. 1, 20 (1938) (*Morgan II*).

The Tax Court procedure is so aberrant that we have found not a single example in which a court of law purported to keep any similar report or findings secret. Indeed, New Jersey Chief Justice Arthur Vanderbilt, a leading administrative law scholar, could not even find such a case a half-century ago, when he condemned a similar practice of secret agency factfinding. As he wrote in another landmark due process case, *Mazza* v. *Cavicchia,* 105 A.2d 545, 557 (N.J. 1954), in which the court held such a practice unconstitutional: "We have not been able to find a single case in any state of the Union, nor have any been cited to us, justifying or attempting to justify the use of secret reports by a hearer to the head of an administrative agency. To approve such a practice in deciding an administrative controversy would be to confer on New Jersey the dubious distinction of being the only jurisdiction in the United States to ignore a fundamental element of due process and fair play." There, as here, the state had argued that it could keep the hearing officer's findings secret because they did not legally bind the agency, the ultimate decisionmaker. But the court held that due process required disclosure and a right to contest the hearing officer's findings before the actual factfinder.

Thus, even in routine and less formal administrative hearings, due process has long required that the parties be provided any reports of the hearing officer who heard the witnesses. These same principles underlie this Court's decision in cases like *Gonzalez* v. *United States*, 348 U.S.

407 (1955). The statute there created a right to a hearing in the Department of Justice (DOJ) for persons who asserted conscientious objections to military service. *Id.* at 412 n.3. Gonzalez was given that hearing, and the DOJ, as required by statute, issued a recommended disposition to the decisionmaker with final authority, the Appeal Board. The report was wholly advisory. Even so, this Court overturned, on constitutional and statutory grounds, the refusal of the Appeals Board, the original factfinder, to disclose that DOJ report to the parties. The Court held that "our underlying concepts of procedural regularity and basic fair play" required that "a copy of the recommendation of the Department be furnished the registrant at the time it is forwarded to the Appeal Board, and that he be afforded an opportunity to reply." *Gonzales*, 348 U.S. at 412. The Court explained: "It is true that the recommendation of the Department is advisory . . .. A natural corollary of this, however, is that a registrant be given an opportunity to rebut this recommendation when it comes to the Appeal Board, the agency with the ultimate responsibility for classification." *Id.* at 412-13.

Thus, if the Special Trial Judge's report had no legal weight at all and were somehow only advisory, due process would then require not only disclosure of those findings but an opportunity to address them before the Tax Court. See also *Morgan* v. *United States*, 304 U.S. 1, 19-20 (1938). Indeed, in every other federal judicial context involving a two-tiered adjudication within a tribunal, the parties are entitled not only to receive the report, findings, or tentative conclusions of the first hearing officer, but, consistent with *Gonzales*, to respond to those materials before the final adjudicator makes a decision.[19]

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[19] See, *e.g.*, 28 U.S.C. § 636(b)(1)(B) (magistrates); FED. R. BANKR. P. 9033; FED. R. CIV. P. 53(f) (special masters); Ct. Int'l Trade R. 53(e); 5 U.S.C. § 557 (agencies).

This requirement only makes sense: if the findings of the trial judge carry legal weight before the Tax Court, the parties are provided a meaningful hearing through their appearance and arguments before the trial judge. But if those findings carry no weight, the trial before the Special Trial Judge provides the parties contesting the facts essentially no meaningful process; the trial judge has no legal power to affect the ultimate decision. In that case, only an adequate process before the Tax Court itself, involving access to the recommended findings and an opportunity to address them, would suffice for due process. It is the opportunity to make one's case before a relevant factfinder that is protected by the due process clause, which is what this Court's decisions in cases like *Gonzalez* hold.

IV. DISCLOSURE OF THE SPECIAL TRIAL JUDGE'S REPORT IS INDEPENDENTLY REQUIRED BY STATUTE.

A. The Rule 183 Report Must be Disclosed by Statute.

1. Even were it not constitutionally required, disclosure of the Special Trial Judge's report would still be mandated by the statutes that govern the Tax Court. At a minimum, these statutes should be construed to avoid the serious due process concerns otherwise raised.

Section 7461(a) of the Code requires that "*all reports* of the Tax Court and all evidence received by the Tax Court * * * shall be public records." 26 U.S.C. § 7461(a) (emphasis added). Similarly, § 7459(b) requires that the Tax Court "shall report in writing *all* its findings of fact, opinions, and memorandum opinions." 26 U.S.C. § 7459(b). (emphasis added). Section 7461 contains only a narrow exception to this obligation of transparency: the Tax Court may exempt from disclosure trade secrets or other confidential information. See 26 U.S.C. § 7461(b).

Special Trial Judge reports are included among "all reports of the Tax Court" within the meaning of the statute. The statute does not refer, as the Government suggests, only to reports issued by the entire Court. See, *e.g.*, *Louisville & N. R. Co.* v. *Comm'r*, 641 F.2d 435, 443 (6th Cir. 1981) (referring to "[t]he initial report of the Tax Court in this case, issued by the assigned special trial judge"). The trial judge's report contains the considered findings and conclusions of an official who has exercised the Tax Court's judicial power in trying the case. *See Freytag*, 501 U.S. at 880-82; 26 U.S.C. §§ 7443, 7443A. That judicial officer issues what the Tax Court's own rules declare to be a "report." Tax Ct. R. 3(d). Section 7461 does not distinguish between final and interim reports, or between internal and external reports. Nothing in the Code authorizes the Tax Court to exempt STJ "reports" from the statutory command that "all reports" of the Tax Court "shall be public records."

And if these reports somehow were not among the reports of the Tax Court covered by the statute, they would have to amount to "evidence" that is considered by that court in rendering its decision and that must be made a public record under Section 7461(a). Because the report of the judge who heard the witnesses is essential to the Tax Court's assessment of their credibility, it is, at the very least, a particularly important piece of evidence before the Tax Court. *Cf. Erhard* v. *Commissioner*, 46 F.3d 1470, 1476 (9th Cir. 1995) (discussing reliance of Tax Court on STJ findings).

The public-records requirement imposed by Congress is broad and cannot be evaded by placing a novel label on a document on which the Tax Court has relied in rendering its decision. Congress specifically and intentionally drafted these transparency requirements to include "all" reports, "all" evidence received, "all" findings of fact, "all" opinions, and "all" memorandum opinions. These statutes require disclosure of the reports of Tax Court trial judges – and

should be construed to do so in light of the due process issues suppression of these reports otherwise presents.

2. Congress enacted these statutes against the longstanding common-law right of access to judicial records. To the extent there is any ambiguity, therefore, the statutes should be construed, consistent with that right, to require disclosure.

The American legal tradition has long recognized a common-law right of access to judicial records and documents. See, *e.g.*, *Nixon* v. *Warner Communications, Inc.*, 435 U.S. 589, 597 (1978) (common-law right). Congress should be presumed aware of this tradition and the common-law right, which "antedates the Constitution." *Bank of Am. Nat'l Trust & Savings Ass'n* v. *Hotel Rittenhouse Assoc.*, 800 F.2d 339, 343 (3d. Cir. 1986). This right, which applies to civil cases,[20] generates a strong presumption of access to "public records and documents, including judicial records and documents." *Nixon*, 435 U.S. at 597. This right exists both to protect the interests of litigants and to secure "the citizen's desire to keep a watchful eye on the workings of public agencies." *Id.* at 598. Indeed, the Tax Court itself has recognized that this right attaches to its own proceedings. "As a general rule, common law, statutory law, and the U.S. Constitution support the proposition that official records of all courts, including this Court, shall be open and available to the public for inspection and copying." *Willie Nelson Music* v. *Comm'r*, 85 T.C. 914, 917 (1985). See also *id.* at 919 ("In these cases, members of the public have an interest in free access to the facts and in understanding disputes that are presented to this forum for resolution. They also have an

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[20] See, *e.g.*, *Publicker Indus., Inc.* v. *Cohen*, 733 F.2d 1059, 1066-67 (3d Cir. 1984); *Smith* v. *United States Dist. Court for the S. Dist. of Ill.*, 956 F.2d 647, 650 (7th Cir. 1992); *Wilson* v. *Am. Motors Corp.*, 759 F.2d 1568, 1570 (11th Cir. 1985).

interest in assuring that courts are fairly run and judges are honest.").

In identifying a "judicial record" to which the presumption of access applies, the overarching principle is that such records consist of all "materials on which a court relies in determining the litigants' substantive rights." *FTC* v. *Standard Fin. Mgmt. Corp.*, 830 F.2d 404, 408 (1st Cir. 1987); see also *United States* v. *El-Sayegh*, 131 F.3d 158, 163 (D.C. Cir. 1997) ("what makes a document a judicial record and subjects it to the common law right of access is the role it plays in the adjudicatory process"); *Smith* v. *United States Dist. Court Officers*, 203 F.3d 440, 442 (7th Cir. 1999) (it is "a right of access to those records of a proceeding that are filed in court or that, while not filed, are relied upon by a judicial officer in making a ruling or decision."); *Smith* v. *United States Dist. Court for the S. Dist. of Ill.*, 956 F.2d 647, 650 (7th Cir. 1992) (granting access to memo sent by Clerk of Court to all judges because, *inter alia*, trial judge specifically stated that he had relied on it in making his decision); *Joy* v. *North*, 692 F.2d 880, 894 (2d Cir. 1982); *Wash. Legal Found.* v. *U.S.S.C.*, 89 F.3d 897, 905 (D.C. Cir. 1996); *United States* v. *Martin*, 749 F.2d 964, 968 (3d Cir. 1984). The common-law right extends even to judicial documents that merely shed light on the bases for judicial decisions. See, *e.g.*, *Brown & Williamson* v. *FTC*, 710 F.2d 1165, 1181 (6th Cir. 1983) (noting public interest "in ascertaining what evidence and records the District Court and this Court have relied upon in reaching our decisions"); *Joy* v. *North*, 692 F.2d at 894 (requiring that "a report" used in rendering judgment be revealed: "[s]ince it is the basis for the adjudication, only the most compelling reasons can justify the total foreclosure of public and professional scrutiny.").

Under these principles, there is little doubt that the press, the public, and the litigants have a common-law right of access to the STJ's report. See, *e.g.*, *Smith*, 203 F.2d at 441

(Posner, J.) ("The public, including the parties to a suit, have a right of access to the records of a judicial proceeding."); see also *Brown & Williamson*, 710 F. 2d at 1177 (acknowledging First Amendment right of access to judicial documents).[21] The STJ's report is more significant than documents that "might" merely have affected a judicial decision. That report contains findings the Tax Court is required to treat as "presumed correct." The Tax Court has never articulated any legitimate interest, or any interest all, for starting to suppress this material in 1983. To the extent unique interests arise in specific cases, such as privacy or trade secrets, ample means to protect those interests exist. See *Nixon,* 435 U.S. at 598 ("access has been denied where court files might have become a vehicle for improper purposes.").

That every federal judicial institution would routinely disclose analogous findings and reports, and that they would be required to do so as a matter of common-law right, counsels in support of construing the Tax Court disclosure statutes to provide access to the STJ reports. See *Nixon,* 435 U.S. at 602.

B. Sections 7461 and 7459 Were Intended To Eliminate Secrecy With Respect To Initial Determinations Like Those Contained In The Special Trial Judge's Report.

As the context in which these provisions were enacted demonstrates, Congress has considered secrecy in tax proceedings a particularly grave problem of public administration virtually since the inception of the income tax. Sections 7461 and 7459 were designed precisely to ensure disclosure of documents involved at all stages of tax proceedings, including documents that contain preliminary findings of fact and conclusions of law.

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[21] The First Amendment issues at stake also counsel in favor of reading the statutes to require disclosure.

Refusal to disclose STJ reports is the type of practice that Congress intended to prevent when it first created the Board of Tax Appeals, the predecessor to the Tax Court. As initially proposed in 1924, the bill to create the Board of Tax Appeals generated intense debate about fair and open process in conflicts between the government and taxpayers. The executive's initial proposal required only that "[t]he proceedings of the Board shall be informal and in accordance with such rules as the Board . . . may prescribe." Dubroff, HISTORICAL ANALYSIS at 60.

A minority, led by Senators Jones and Walsh, objected vehemently and proposed a floor amendment:

> "Under the present practice all [resolutions of tax disputes] are made in secret. An opportunity is afforded for favoritism, arbitrary action, fraud, and collusion. * * * *The majority proposes that all records and proceedings of the Internal Revenue Bureau shall remain secret as in the past.* To the minority it seems inconceivable that any controversy existing between the Government and a taxpayer should be adjudicated and finally determined in a star chamber proceeding. The minority will, therefore, propose an amendment to the bill which will provide that *all such proceedings, records, and evidence in connection therewith shall be public.*"

S. Rep. No. 68-398, pt. 2, at 12 (1924) (emphasis added).

The Jones-Walsh amendment contained substantially the same transparency language that now exists in Sections 7461 and 7459.[22] The purpose was to ensure that all phases in the

[22] As enacted the statute read in relevant part: "It shall be the duty of the board . . . to make a report in writing of its findings of fact and decision in each case a copy of its report shall be entered of record and a copy furnished the taxpayer. . . . All reports of the Board . . . and all evidence received by the Board . . . shall be

adjudication of tax disputes would be subject to public scrutiny, for the benefit of both taxpayers directly affected and for public assessment of tax controversies more generally. As one sponsor put it: "[I]t is of much greater concern that those judicial proceedings should be public and become permanent records and open to a public inspection, so that we may understand the facts upon which decisions are reached, and the taxpayers in the country may have an opportunity to know just how it all happens." Cong. Rec. S. 8133 (1924) (Sen. Jones). As the other sponsor said: "the proceedings ought to approximate as nearly as practicable to proceedings in court." Id. (Sen. Walsh).

The Senate debates underscore the aim of abolishing all vestiges of secrecy. Senator LaGuardia observed that the "board of appeals and the publicity placed upon its activities are the result of the vicious secrecy system which has grown up in the Treasury Department under the present law." 65 Cong. Rec. 9549 (1924). Most importantly, this requirement of transparency applied not only to final proceedings, but to *every* stage of tax litigation. Senator Jones stated that:

> whenever there is a controversy between the Government and a taxpayer, *the proceedings leading up to that decision should be public proceedings*. [Proceedings and records should be] open to a public inspection, so that we may understand *the facts upon which decisions are reached*, and the taxpayers in the country may have an opportunity to know just how it all happens.

65 Cong. Rec. 8132-34 (emphasis added). Accordingly, the Senate Report was clear that the enacted disclosure requirements encompassed not only final decisions of the

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public records open to the inspection of the public. . . . " Section 901(h) of the Revenue Act of 1924, Pub. Law No. 68-176.

Board, but all "records * * * in connection therewith." S. Rep. No. 68-398, pt. 2, at 12 (1924).

At the time of the adoption of Section 7461, the "reports" of the Board of Tax Appeals had less legal weight than the Special Trial Judge's reports do today. "The hearing before the Board was at that time little more than a preliminary skirmish, a run for luck. For either party, if dissatisfied with the decision, could bring a court action and try the matter de novo, the Board's findings of fact being prima facie evidence against the losing party." *Blair* v. *Curran*, 24 F. 2d 390, 392 (1st Cir. 1928). That Congress intended for publication of such findings to be mandatory is further reason that Sections 7461 and 7459 should be construed to require disclosure of the STJ reports today.

V. THIS COURT SHOULD EXERCISE ITS SUPERVISORY POWER TO REQUIRE DISCLOSURE OF THE SPECIAL TRIAL JUDGE'S REPORT.

Finally, this case calls for an exercise of this Court's supervisory power over the federal courts, appropriate when the lower courts have "so far departed from the accepted and usual course of judicial proceedings, or sanctioned such a departure by a lower court . . .." S.Ct. R. 10(a).

"The authority which Congress has granted this Court to review judgments of the courts of appeals undoubtedly vests us not only with the authority to correct errors of substantive law, but to prescribe the method by which those courts go about deciding the cases before them." *Lehman Brothers* v. *Schein*, 416 U.S. 386, 393 (1974) (Rehnquist, J., concurring); see also 28 U.S.C. § 2106. As the Court recently noted, "this Court can establish rules of 'sound judicial practice'" through the exercise of "supervisory power" over the courts whose decisions are subject to its review. *Intel Corp* v. *Advanced Micro Devices, Inc.*, 124 S. Ct. 2466, 2483 (2004) (quoting *Thomas* v. *Arn*, 474 U.S. 140, 146-47 (1985)). This Court is

empowered to impose on the lower courts "procedures deemed desirable from the viewpoint of sound judicial procedure though in nowise commanded by statute or by the Constitution." *Thomas*, 474 U.S. at 146-47. This supervisory power focuses on "the need to protect the integrity of the federal courts," see, *e.g.*, *United States* v. *Payner*, 447 U.S. 727, 736 n.8 (1980), and to secure "the public reputation of judicial proceedings." *Nguyen* v. *United States*, 123 S. Ct. 2130, 2139 n.17 (2003).

In *Nguyen*, the Court employed its supervisory power to invalidate the judicial practice at issue even without a showing of individual prejudice to the specific defendant. That approach should apply *a fortiori* to a situation in which the court of appeals has decided a case without access to the trial judge's findings of fact to the actual prejudice of the appellate court's ability properly to render a "judicial" decision. This Court should not permit the courts of appeals to review decisions from the Tax Court on the basis of an incomplete record that lacks the findings of the one judge who heard the witnesses and presided at trial.

To attempt to engage in the appellate function without access to the trial judge's report, as the court below was forced to do by the Tax Court's refusal to provide that report, so far departs from the "accepted and usual" course of judicial proceedings – indeed, from the proceedings of every other court – as to warrant exercise of this Court's supervisory power. So too does the process within the Tax Court of refusing to disclose to the parties or the reviewing court the trial judge's findings and report.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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Dated: August 2, 2004

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 03-61075

In Re: ESTATE OF ROBERT W. LISLE; ESTATE OF DONNA M. LISLE; THOMAS W. LISLE, Independent Co-Executor; AMY L ALBRECHT, Independent Co-Executor,

Petitioners,

Petition for Writ of Mandamus
to the
United States Tax Court

Before JOLLY, SMITH, and WIENER, Circuit Judges.

BY THE COURT:

IT IS ORDERED that the Petitioners-Appellants' Motion to Enforce This Court's Mandate, treated as a petition for write of mandamus, is DENIED.

Although Petitioners-Appellants present a compelling case that, on remand from our opinion filed July 30, 2003, the Tax Court's stated intention to "add new penalties based on negligence, substantial understatement of income and tax-motivated interest" will exceed the strictures of our limited mandate, we remain mindful of the Supreme Court's admonition that mandamus is not to be used as a substitute for appeal. Despite the implication of the Tax Court's orders

of November 19, 2003, and the inferences reasonably drawn therefrom by Petitioners-Appellants, that Court has not issued its final judgment. Thus it is impossible to tell whether, on remand, the Tax Court will in fact exceed the narrow limits of our remand, which permits only a recalculation of tax in light of that portion of the Tax Court's original judgment that we reversed. If, in the certain knowledge that its impending judgment whether it exceeds our mandate on remand, the Tax Court does – as appellants suggest – "go much further," that contention can be dealt with in the appellate process. We trust that, in the final analysis, the Tax Court will not make yet another reversal necessary.

MOTION DENIED.

U.S. COURT OF APPEALS
FILED
JAN 7 2004
CHARLES R. FULBRIDGE III
CLERK

UNITED STATES TAX COURT
WASHINGTON, DC 20217

ESTATE OF ROBERT W. LISLE, DECEASED, THOMAS W. LISLE AND AMY L. ALBRECHT, INDEPENDENT CO-EXECUTORS, AND ESTATE OF DONNA M. LISLE, DECEASED, THOMAS W. LISLE AND AMY L. ALBRECHT, INDEPENDENT CO-EXECUTORS,

Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

Docket No. 215555-91.

ORDER

On July 30, 2003, the United States Court of Appeals for the Fifth Circuit filed its Judgment in this case, and issued its mandate on September 23, 2003, affirming in part and reversing in part the Decision of this Court entered on July 24, 2001, and remanding the case to this Court for further proceedings in accordance with its Opinion.

The Court of Appeals reversed this Court's finding of fraud with respect to Estate of Robert W. Lisle's additions to tax under section 6653 (b) (1) (A) and (B), Internal Revenue Code, for 1987. However, the Court of Appeals sustained our decision with respect to petitioners' Federal income tax deficiency for 1987. In doing so, the Court of Appeals remanded this case for the limited purpose of recalculating the deficiency and additions to tax, consistent with its Opinion.

Respondent determined in the notice of deficiency dated July 24, 1991, that petitioners were liable for additions to tax for negligence under section 6653 (a) (1) (A) and (B), under section 6661 (a) for a substantial understatement of income, and under section 6621 (c) for additional interest. In the Amendment to Answer filed on July13, 1994, respondent claimed alternatively that these additions to tax and interest, as increased, were due from petitioners in the absence of fraud. Consequently, it is our view that the final decision to be entered in this case should include the amounts of any additions to tax and section 6621 (c) interest that are applicable. Accordingly, it is

ORDERED:

1. That on or before December 29, 2003, the parties are directed to submit an agreed decision to be entered by the Court.

2. That, if the parties are unable to agree on a proposed decision, they are directed to file separate computations and a memorandum explaining their differences.

(signed) HOWARD A. DAWSON, JR.

Howard A. Dawson, Jr.
Judge

Dated: Washington, D.C.
November 19, 2003

Docket Nos. 43966-85, 712-86, 45273-86, 1350-87, 31301-87, 33557-87, 3456-88, 30830-88, 32103-88, 27444-89, 16421-90, 25875-90, 26251-90, 20211-91, 20219-91, 21555-91, 21616-91, 23178-91, 24002-91, 1984-92, 16164-92, 19314-92, 23743-92, 26918-92, 7557-93, 22884-93, 25976-93 and 25981-93

UNITED STATES TAX COURT

INVESTMENT RESEARCH ASSOCIATES, LTD., AND SUBSIDIARIES, et al.,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECLARATION OF RANDALL G. DICK

Randall G. Dick, for his Declaration under penalty of perjury, pursuant to 28 U.S.C. 1746, states as follows:

1. I am of full age, and if called to testify, would be competent to give the testimony as to the following matters.

2. I am counsel for Investment Research Associates, Ltd. and Subsidiaries and for Burton and Naomi Kanter.

3. In its Opinion in this matter filed on December 15, 1999 (T.C. Memo 1999-407) the U.S. Tax Court concluded, with respect to issue 1, that payments made by Hyatt, Frey, Schaffel, Schnitzer and Eulich (the "Five") were taxable to the individual Petitioners and the individual Petitioners were liable for the fraud additions to tax and penalty with respect to such income. (Opinion, 226-319).

4. Subsequent to the issuance of the Tax Court's Opinion, Declarant was informed by two judges of the Tax Court, that in his original report submitted to the Chief Judge pursuant to Rule 183(b), Special Trial Judge D. Irwin Couvillion concluded that payments made by the Five were not taxable to the individual Petitioners and that the fraud penalty was not applicable.

5. In my conversations with the judges of the Tax Court, I was told the following: That substantial sections of the opinion were not written by Judge Couvillion, and that those sections containing findings related to the credibility of witnesses and findings related to fraud were wholly contrary to the findings made by Judge Couvillion in his report. The changes to judge Couvillion's findings relating to credibility and fraud were made by Judge Dawson.

6. Judge Dawson`s revisions resulted in a finding that over nine million dollars is taxable to the individual Petitioners. This finding based upon credibility of witnesses, results in liability of the individual Petitioners for tax, penalties and interest in an amount in excess of $30,000,000.

7. I confirmed the information, in paragraphs 4 and 5 above with another judge of this Court, who informed me that in fact, the Opinion was changed, and that to his knowledge, it was the first time the Tax Court had made an outright rejection of credibility findings made by a Special Trial judge.

8. I was also told by a judge of the Tax Court that the changed sections of the report were written in such a way so that wherever there was the "slightest issue of doubt, it went against" the Petitioners.

I declare under penalty of perjury that the foregoing is true and correct and that this Declaration is executed in San Francisco, California on August 21, 2000.

RANDALL G. DICK

Supreme Court, U.S.
FILED
OCT 12 2004
OFFICE OF THE CLERK

Nos. 03-184 and 03-1034

In the Supreme Court of the United States

CLAUDE M. BALLARD AND MARY B. BALLARD,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ESTATE OF BURTON W. KANTER, ET AL.,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON WRITS OF CERTIORARI
TO THE UNITED STATES COURTS OF APPEALS
FOR THE ELEVENTH AND SEVENTH CIRCUITS

BRIEF FOR THE RESPONDENT

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QUESTIONS PRESENTED

When a case is assigned to a special trial judge of the United States Tax Court, the special trial judge is required to make a "report, including findings of fact and opinion, to the Chief Judge, and the Chief Judge will [then] assign the case to a Judge or Division of the Court." Tax Ct. R. 183(b). The Judge to whom the case is assigned "may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part." Tax Ct. R. 183(c). The questions presented are:

1. Whether the Due Process Clause requires that the "original" report of a special trial judge be made public by inclusion in the record so as to facilitate appellate review.

2. Whether 26 U.S.C. 7459(b), 7461(a), (b), or 7482 requires that the "original" report of a special trial judge be made public by inclusion in the record so as to facilitate appellate review.

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In the Supreme Court of the United States

No. 03-184

CLAUDE M. BALLARD AND MARY B. BALLARD, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

No. 03-1034

ESTATE OF BURTON W. KANTER, ET AL., PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON WRITS OF CERTIORARI TO THE UNITED STATES COURTS OF APPEALS FOR THE ELEVENTH AND SEVENTH CIRCUITS

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the court of appeals in No. 03-184 (Ballard) (Pet. App. 1a-18a) is reported at 321 F.3d 1037. The opinion of the Tax Court (Pet. App. 19a-306a) is unofficially reported at 78 T.C.M. (CCH) 951.

The opinion of the court of appeals in No. 03-1034 (Kanter) (Pet. App. 1a-97a) is reported at 337 F.3d 833. The opinion of the Tax Court (Pet. App. 98a) is unofficially reported at 78 T.C.M. (CCH) 951.

JURISDICTION

The judgment of the court of appeals in No. 03-184 was entered on February 13, 2003. A petition for rehearing was denied on May 5, 2003 (Pet. App. 307a). The petition for a

writ of certiorari was filed on August 4, 2003, and was granted on April 26, 2004.

The judgment of the court of appeals in No. 03-1034 was entered on July 24, 2003. A petition for rehearing was denied on October 21, 2003 (Pet. App. 115a). The petition for a writ of certiorari was filed on January 20, 2004, and was granted on April 26, 2004.

The jurisdiction of this Court rests on 28 U.S.C. 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Fifth Amendment to the United States Constitution is set forth at 03-1034 Pet. App. 116a. Sections 7443A, 7459(a) and (b), 7461(a), and 7482(a)(1) of the Internal Revenue Code, 26 U.S.C. 7443A, 7459(a) and (b), 7461(a), 7482(a)(1), and Tax Court Rule 183 are set forth in the appendix to this brief. App., *infra*, 1a-9a.

STATEMENT

Under Section 7443A(b)(4) of the Internal Revenue Code, the Chief Judge of the United States Tax Court may designate a special trial judge (STJ) to hear, but not decide, any proceeding. Where an STJ hears a case under that provision, Tax Court Rule 183 requires the STJ to prepare and submit a report of the proceeding, including recommended factual findings and legal conclusions, to the Chief Judge, who then assigns the case for decision to a regular judge of the Tax Court. See Tax Ct. R. 183(b). The judge to whom the case is assigned "may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part," and gives "[d]ue regard" to the STJ's role as hearing examiner and "presum[es]" that the STJ's factual findings are "correct." Tax Ct. R. 183(c).

In the proceedings below, the courts of appeals held that where a regular Tax Court judge adopts an STJ's report and publishes the report in an opinion, any "original" report that

the STJ may have submitted that differs from the STJ's final published report need not be disclosed to the parties or included in the record. Those decisions are correct: Well-settled principles of constitutional law and the longstanding interpretation of Tax Court procedures make clear that such disclosure is not required.

1. The Tax Court was first established in 1924 as the Board of Tax Appeals, an independent agency in the executive branch of the Government that exercised limited jurisdiction over certain tax disputes prior to the payment of the disputed tax. See Revenue Act of 1924, ch. 234, § 900(h), 43 Stat. 337. The Board became the Tax Court of the United States in 1942, see Revenue Act of 1942, ch. 619, § 504(a), 56 Stat. 957, but remained an executive agency until 1969. In that year, Congress formed the modern Tax Court as a legislative tribunal under Article I of the Constitution with authority to adjudicate specific income, estate, and gift tax disputes before payment of the tax. See Tax Reform Act of 1969, Pub. L. No. 91-172, § 951, 83 Stat. 730; 26 U.S.C. 7441. The court is composed of 19 regular judges who are appointed for 15-year terms but may be removed by the President for "inefficiency, neglect of duty, or malfeasance in office," 26 U.S.C. 7443(e) and (f), and several STJs who are periodically appointed by the Chief Judge. See Tax Reform Act of 1984, Pub. L. No. 98-369, § 464(a), 98 Stat. 824; 26 U.S.C. 7443A(a).

STJs have statutory authority to hear cases and enter the decision of the Tax Court in declaratory judgment proceedings, "small tax cases," and levy and lien proceedings. See 26 U.S.C. 7443A(b)(1)-(3) and (c) (1994). STJs may also exercise authority under Section 7443A(b)(4) of the Internal Revenue Code to "hear" "any other proceeding which the chief judge may designate," but may not enter decisions in those cases.

See 26 U.S.C. 7443A(b)(4) and (c) (1994).[1] If an STJ hears a case pursuant to Section 7443A(b)(4), Tax Court Rule 183 requires the STJ to prepare a report, which is transmitted to the Chief Judge of the Tax Court, who then assigns the case to a regular Tax Court judge for decision. See Tax Ct. R. 183(b). The Tax Court judge may "adopt the Special Trial Judge's report" or "modify it" or "reject it in whole or in part," and gives "[d]ue regard * * * to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Tax Ct. R. 183(c).

2. This case arises out of a tax dispute between the government and Burton Kanter, Claude Ballard, and a third party, Robert Lisle. The late Burton Kanter was a well-known attorney and academic with expertise in federal income and estate taxation. 03-184 Pet. App. 45a-46a.[2] Claude Ballard is a former senior vice-president of Prudential Insurance Co. of America (Prudential), a position in which he exercised influence over Prudential's purchase and development of real estate, as well as Prudential's choice of builders and contractors for construction projects. *Id.* at 46a-47a. Like Ballard, Robert Lisle was a former Prudential vice-president, a capacity in which he exercised authority over

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[1] Section 7443A(b)(4) has been re-designated as 26 U.S.C. 7443A(b)(5). See Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, § 3401(c), 112 Stat. 749-750. Because this case was decided under the previous version of the Code, we will refer only to that version in this brief.

[2] As the court below observed, "from 1979 to 1989 Kanter, the highly successful tax attorney, who hobnobbed with Pritzkers and Hollywood producers and who participated in countless extremely large and lucrative business ventures, reported a negative adjusted gross income each year on his federal tax return and paid no federal income taxes." 03-1034 Pet. App. 2a-3a.

the award of Prudential loans and construction contracts. *Id.* at 47a.

Sometime between 1968 and 1970, Kanter met Ballard and Lisle, and the three agreed that Kanter would sell Ballard's and Lisle's influence over Prudential business and launder the proceeds through a complex network of corporations and trusts controlled by them. 03-184 Pet. App. 48a. Specifically, Kanter arranged for five individuals seeking Prudential business to pay kickbacks to an entity he controlled, called Investment Research Associates, Ltd. (IRA), or to one of IRA's subsidiaries, and those funds would then be commingled with other money in an account controlled by a different Kanter entity. *Id.* at 48-49a. Some of the funds were then distributed to Kanter, Ballard, and Lisle as "commissions, consulting fees, or directors fees." *Id.* at 49a. Larger portions of the payments were "distributed to three of IRA's subsidiaries; more specifically, 45 percent to Carlco, Inc. (Carlco) (controlled by Lisle), 45 percent to TMT, Inc. (TMT) (controlled by Ballard), and 10 percent to BWK, Inc. (controlled by Kanter)." *Ibid.* By the end of 1983, IRA had accumulated $4,771,445 in payments from the five bribers, which were distributed in the 45-45-10 ratio to TMT, Carlco, and BWK but not reported on Kanter's, Ballard's, or Lisle's tax returns. *Id.* at 5a.

After discovering the scheme, the Commissioner of Internal Revenue issued notices of deficiency to Ballard, Kanter, and Lisle, seeking unpaid taxes and, later, civil fraud penalties in connection with the millions of dollars of unreported kickbacks. 03-184 Pet. App. 5a. All three sought review in the Tax Court, and their cases were consolidated for hearing before STJ D. Irvin Couvillion pursuant to Section 7443A(b)(4). *Id.* at 33a. After a lengthy trial, in which thousands of exhibits consuming hundreds of thousands of pages were placed in evidence, STJ Couvillion submitted a report of the proceedings to then-Chief Judge

Cohen, who referred the case to Tax Court Judge Howard A. Dawson for decision. *Id.* at 5a-6a, 311a; 03-1034 Pet. App. 3a.

On December 15, 1999, Judge Dawson issued an opinion for the Tax Court, holding Kanter, Ballard, and Lisle liable for underpaid taxes and assessing a fraud tax penalty against them. 03-184 Pet. App. 19a-306a. Judge Dawson's opinion states that the Tax Court "agrees with and adopts the opinion of the Special Trial Judge," which the court "set[s] forth" in the margin of its opinion. *Id.* at 33a. The STJ opinion, in turn, analyzes the documentary and other evidence in painstaking detail and carefully traces the millions of dollars paid to IRA and its subsidiaries through the web of corporations and entities controlled by Kanter, Ballard, and Lisle, see *id.* at 49a-229a. The STJ opinion concludes that Kanter, Ballard, and Lisle had "entered into arrangements pursuant to which [Kanter] would use his business and professional contacts, including his relationships with * * * Ballard, and Lisle, to assist individuals and/or entities in obtaining business opportunities or in raising capital for business ventures" with Prudential in return for kickbacks, which Kanter would launder through "a complex organization of corporations, partnerships, and trusts," but not report as income for tax purposes. *Id.* at 48a.

3. On April 20, 2000, Kanter, Ballard, and Lisle filed a motion seeking access to "all reports, draft opinions or similar documents prepared and delivered to the Court pursuant to Rule 183(b)" by STJ Couvillion, or in the alternative for the court to include a copy of those materials in the record transmitted to the appellate court. 03-1034 Pet. App. 107a-108a.

The Tax Court denied the motion. 03-1034 Pet. App. 107a-112a. It observed that STJ Couvillion's report "ultimately became the Memorandum Findings of Fact and Opinion (T.C. Memo. 1999-407) filed on December 15, 1999," see *id.* at 108a, and that the procedures followed in the case complied

with Internal Revenue Code Section 7443A(b)(4) and Tax Court Rule 183. *Id.* at 108a-109a. Because the STJ lacked authority "actually to decide" the case, moreover, the Tax Court concluded that the motion amounted to an improper request for access to "confidential" materials that "relate to the internal deliberative processes of the Court." *Id.* at 109a.

Ballard, Kanter, and Lisle subsequently filed a motion for reconsideration, citing an affidavit from Randall G. Dick, counsel for Kanter. 03-1034 Pet. App. 99a-100a, 101a. The affidavit asserts that two or three judges of the Tax Court had informed counsel that the "original report" that STJ Couvillion submitted to the Chief Judge concluded, contrary to the report ultimately set forth in the Tax Court's decision, that the petitioners should not have been assessed a tax or a fraud penalty. *Id.* at 101a-102a.

In an opinion signed by Chief Judge Wells, Judge Dawson and STJ Couvillion, see 03-184 Pet. App. 315a-316a, the court again denied the motion. *Id.* at 312a-316a. The court's order states that "[t]he only official Memorandum Findings of Fact and Opinion by the Court in these cases is T.C. Memo. 1999-407, filed on December 15, 1999, by Special Trial Judge Couvillion, reviewed and adopted by Judge Dawson, and reviewed and approved by former Chief Judge Cohen." *Id.* at 314a-315a.

4. Ballard, Kanter, and Lisle immediately filed petitions for mandamus in the Eleventh, Seventh, and Fifth Circuits, respectively, seeking an order directing the Tax Court to provide them with a copy of the "original" report prepared by STJ Couvillion. The petitions for writs of mandamus were denied. *In re Ballard*, No. 00-14762-H (11th Cir. Oct. 23, 2000); *In re Investment Research Ass'ns*, No. 00-3369 (7th Cir. Dec. 15, 2000); *In re Estate of Lisle*, No. 00-60637 (5th Cir. Sept. 18, 2000).

Ballard, Kanter,[3] and Lisle subsequently filed appeals in the Eleventh, Seventh, and Fifth Circuits, respectively. All three courts of appeals concluded that the taxpayers are not entitled to any "original report" of STJ Couvillion. 03-184 Pet. App. 1a-18a; 03-1034 Pet. App. 1a-97a; *Estate of Lisle* v. *Commissioner*, 341 F.3d 364 (5th Cir. 2003).

a. **No. 03-184.** The Eleventh Circuit, considering Ballard's appeal, affirmed the Tax Court's decision in its entirety. 03-184 Pet. App. 1a-17a. With respect to Ballard's argument that the Tax Court unconstitutionally withheld "the findings of the [STJ]" from the parties, *id.* at 2a, the court of appeals concluded that the argument was incorrectly "premised upon the assertion that the underlying report adopted by the Tax Court is not, in fact, [STJ] Couvillion's report." *Id.* at 9a. In the Eleventh Circuit's view, the record belied that assumption as it "clearly reveals that the report adopted by the Tax Court is [STJ] Couvillion's report." *Ibid.*

Even if the STJ had initially filed a report with the Chief Judge that differed from the final report adopted by the Tax Court, non-disclosure of the initial report would "not give rise to due process concern." 03-184 Pet. App. 9a. The court reasoned that:

> [T]here is nothing unusual about judges conferring with one another about cases assigned to them. These conferences are an essential part of the judicial process when, by statute, more than one judge is charged with the responsibility of deciding the case. And, as a result of such conferences, judges sometimes change their original position or thoughts. Whether Special Trial Judge Couvillion prepared drafts of his report or subsequently changed his opinion entirely is without import insofar as

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[3] Kanter died on October 31, 2001, and his estate has been substituted as petitioner in his case. 03-1034 Pet. App. 1a.

> our analysis of the alleged due process violation pertaining to the application of Rule 183 is concerned. Despite the invitation, this court will simply not interfere with another court's deliberative process.

Id. at 9a-10a. With respect to Ballard's challenges to the sufficiency of the evidence, the court of appeals held that "[t]he record supports" the imposition of taxes and a fraud penalty for the kickbacks. *Id.* at 14a.

b. **No. 03-1034.** The Seventh Circuit similarly affirmed the decision of the Tax Court with respect to Kanter. 03-1034 Pet. App. 1a-70a. The court of appeals rejected the argument that the "STJ's original report must be made a part of the record on appeal" in order to "determine whether the appropriate degree of deference had been paid to it by the Tax Court judge." *Id.* at 6a. In the Seventh Circuit's view, the argument was "immaterial" because "the underlying report adopted by the Tax Court was in fact Special Trial Judge Couvillion's." *Id.* at 7a. As a result, "[a]ny differing preliminary recommendations [by the STJ]—if they ever existed—would no longer be constitutionally relevant because the STJ has abandoned them." *Id.* at 13a.

Considering Kanter's claim that the judicial deliberations of the Tax Court were "quasi-collaborative" such that "an STJ's initial findings are malleable," the court of appeals concluded that such a system "would not offend our notions of fundamental fairness, nor would due process require the inclusion of the report in the appellate record to preserve the fairness of our review." 03-1034 Pet. App. 7a. Rather, "Congress intended STJ reports to be treated as preliminary findings comprising part of the Tax Court's internal deliberative process." *Id.* at 9a. Turning to the merits, the court of appeals concluded that the Tax Court's findings were not clearly erroneous and affirmed its legal conclusions.

Judge Cudahy concurred in part and dissented in part. 03-1034 Pet. App. 70a-97a. Judge Cudahy read the record to

support "the notion that the Tax Court engages in a quasi-collaborative process of review of the STJ's report from which a new and frequently different STJ's opinion emerges to be adopted and agreed with by the Tax Court." *Id.* at 74a. Although agreeing that such a collaborative procedure does not violate Tax Court Rule 183, see *id.* at 79a-80a, Judge Cudahy opined that such a process violates due process because it deprives the parties of "meaningful appellate review," *id.* at 96a, namely a determination of whether the Tax Court properly deferred to the STJ's credibility findings. *Id.* at 88a-97a.

c. Although its decision is not before the Court, the Fifth Circuit in *Estate of Lisle* v. *Commissioner*, 341 F.3d 364, 384 (2003), also concluded that "application of Rule 183 in this case did not violate Appellants' due process rights" based on "the reasoning of the Seventh and Eleventh Circuits." On the merits of Lisle's claim, the court of appeals concluded that the Commissioner had not carried his burden of establishing fraud with respect to Lisle and reversed the fraud penalties assessed by the Tax Court. *Id.* at 385.

SUMMARY OF ARGUMENT

I. A. Petitioners' primary contentions—that disclosure of the STJ's report is constitutionally and statutorily mandated in order to permit full appellate review and to ensure that the Tax Court has reviewed the STJ's recommended findings under a deferential standard—are not properly presented in these cases. STJ Couvillion's final report was adopted in full by the Tax Court, disclosed to the parties, and included in the record of this case. Accordingly, this case does not present any question concerning the proper degree of deference to be given an STJ's recommendations, nor does it present the question whether disclosure of reports reflecting an STJ's final recommendations is required. Rather, the only question is whether disclosure of an "original" report that was filed with the Chief Judge and later abandoned by

the STJ is required by the Due Process Clause or federal statute. It is not.

B. It is well settled that disclosure of a judge's deliberative processes is shielded from discovery by the parties. Petitioners attempt to divine some special reason for disclosing STJ Couvillion's deliberative process by asserting that the STJ was improperly influenced, but that claim lacks evidentiary support. Indeed, because this Court presumes that judges do not engage in misconduct, petitioners cannot be permitted to probe the STJ's deliberative process in the hope of discovering improper conduct.

Petitioners could gain nothing from mere disclosure of any "original" STJ report, because, as the findings below make clear, the published report accurately reflects the STJ's final recommended disposition of the case. Any differences between that final report and an "original" recommendation —like differences between a draft and final opinion—would not demonstrate improper influence or a failure to defer to the STJ's recommendations, but would presumptively be the result of the STJ's legitimate reevaluation of the case. Petitioners could not hope to substantiate their allegations of improper influence without still further intrusive discovery such as depositions of the judges involved, a result that is barred by precedent.

II. A. Even if presented in this case, petitioners' disclosure arguments would fail. Non-disclosure of the STJ's report does not preclude effective appellate review, because an STJ does not function as a trial court judge whose factual recommendations must be accepted on appeal absent "clear error." To the contrary, in cases such as this, STJs are prohibited by statute from functioning as original finders of fact.

The drafting history of Tax Court Rule 183 demonstrates that Rule 183 was designed to eliminate disclosure and appellate-style review of STJ reports. The "due regard" and

"presumed to be correct" language on which petitioners rely does not give rise to an enforceable right to appellate review, but rather guides the judges of the Tax Court in a way that reflects that the STJ had the opportunity to hear witnesses. Indeed, that language was added as part of an amendment intended to *expand* the Tax Court's options with respect to STJ reports, not limit its discretion over them.

B. The Tax Court's procedures comport with due process. This Court has held that tax disputes involve "public rights," and thus the full panoply of Article III protections is not required here. Nor is the Tax Court's non-disclosure practice unique, as petitioners mistakenly contend. Indeed, Congress has long mandated a similar practice with respect to decisions of regular Tax Court judges that are subject to full court review. Similarly, agency boards of contract appeals generally do not disclose the initial proposed dispositions of presiding judges who actually receive evidence.

In any event, mere novelty would not render the Tax Court's rules unconstitutional. The available evidence suggests that the Tax Court eliminated its disclosure requirement in 1984 to unify the court's decisional process and accommodate a tremendous influx of tax-shelter cases in the mid-1980s. Due process does not foreclose such procedural innovations.

C. Disclosure of the STJ's credibility assessments is unnecessary to prevent the Tax Court from rejecting those assessments "without seeing and hearing the witness" in violation of *United States* v. *Raddatz*, 447 U.S. 667, 681 n.7 (1980). In noncriminal, administrative cases, this Court has rejected claims that due process requires a non-Article III decisional authority to defer to a hearing officer's factual determinations or hear evidence firsthand. In any event, Tax Court Rule 183 contains the sorts of safeguards identified in *Raddatz* as sufficient to permit de novo review of a hearing examiner's credibility assessments.

D. The Tax Court's rules are not invalid under *Mathews* v. *Eldridge*, 424 U.S. 319 (1976). Petitioners have no legitimate interest in the disclosure of internal judicial deliberations, and petitioners' broader interest in the fair adjudication of their claims is amply protected by the procedural protections afforded. Any interest in disclosure would not outweigh the government's substantial interests in ensuring considered and confidential judicial decisionmaking and promoting expeditious resolution of tax cases.

III. The Internal Revenue Code does not compel disclosure of STJ reports. The appellate review provision, 26 U.S.C. 7482(a)(1), merely provides that Tax Court decisions are not entitled to any special deference, but are reviewed in the same manner as district court decisions. With respect to the Code's disclosure provisions, the Tax Court is required to publish an STJ report to the extent the court adopts the report's findings of fact and conclusions of law, see 26 U.S.C. 7459(b), 7461, but the provisions, by their terms, require no further disclosure.

ARGUMENT

I. PETITIONERS' CHALLENGES TO THE TAX COURT'S PRACTICES ARE NOT PROPERLY PRESENTED IN THESE CASES

A. The STJ's Recommended Findings Were Not Reversed Or Set Aside, But Were Instead Adopted And Disclosed In The Tax Court's Decision

Petitioners' primary challenges to the decisions below rest on the premise that disclosure of the STJ's "original" report is necessary to permit meaningful appellate review and to determine whether the Tax Court judge gave proper deference to the STJ's recommended findings. According to petitioners, the Tax Court "revers[ed] critical findings of fact, including credibility judgments, of the judge who had tried the case" (03-1034 Br. 1), but by preserving the confidential-

ity of its decisional process the Tax Court has made it "impossible for any reviewing Article III court to determine if" the Tax Court judge "did indeed give 'due regard' to" the STJ's recommendation (03-184 Br. 19).

The first, and most basic, flaw in petitioners' arguments is that they ignore the actions actually taken by the Tax Court. As we explained at the certiorari stage (03-184 Br. in Opp. 13; 03-1034 Br. in Opp. 12-13, 17), the findings of the Tax Court, affirmed on appeal by three appellate courts, conclusively establish that the Tax Court *accepted* the recommendations of the STJ, *adopted* his final report, and disclosed it by publishing it as the opinion of the court. See 03-184 Pet. App. 33a-306a. Thus, this case does not properly present the questions of what deference, if any, the Tax Court should give an STJ's recommendations before *rejecting* them or whether disclosure of an STJ's report is necessary to permit appellate review of a Tax Court judge's *rejection* of such a report. Resolution of those questions must "await a day when the issue[s] [are] posed less abstractly." *The Monrosa* v. *Carbon Black, Inc.*, 359 U.S. 180, 184 (1959).

It is beyond dispute that the Tax Court's opinion contains an accurate and full reproduction of the final STJ report reflecting the STJ's final recommendations. An order in the record signed by Chief Judge Wells, Judge Dawson, *and* STJ Couvillion provides that the Tax Court "*adopted* the findings of fact and opinion of Special Trial Judge Couvillion" and that "[t]he *only* official Memorandum Findings of Fact and Opinion" in the case was the report "filed on December 15, 1999, by Special Trial Judge Couvillion, reviewed and *adopted* by Judge Dawson, and reviewed and *approved* by former Chief Judge Cohen." *Id.* at 314a-315a (emphasis added). The order further explains that:

> Judge Dawson states and Special Trial Judge Couvillion agrees, that, after a meticulous and time-consuming review of the complex record in these cases, Judge

> Dawson adopted the findings of fact and opinion of Special Trial Judge Couvillion, that Judge Dawson presumed the findings of fact recommended by Special Trial Judge Couvillion were correct, and that Judge Dawson gave due regard to the circumstance that Special Trial Judge Couvillion evaluated the credibility of witnesses.

Id. at 315a.

Consistent with this order, the courts of appeals *uniformly* concluded that the report attributed to STJ Couvillion in the Tax Court's opinion is his report and that its presence in the record disposed of petitioners' claims. 03-1034 Pet. App. 7a ("[W]e accept as true the Tax Court's statement that the underlying report adopted by the Tax Court was in fact Special Trial Judge Couvillion's. This renders moot all of Kanter's arguments.") (internal citations omitted); 03-184 Pet. App. 9a ("[C]ontrary to Petitioners-Appellants' assertions, the record as presented to us clearly reveals that the report adopted by the Tax Court is Special Trial Judge Couvillion's report."); *Estate of Lisle* v. *Commissioner*, 341 F.3d 364, 384 (5th Cir. 2003) (adopting this reasoning).

The express statement by STJ Couvillion and Judge Dawson that the STJ's ultimate recommended findings were adopted by the Tax Court compels rejection of petitioners' repeated claims that the STJ's "report remains secret to this day—even from this Court" (03-184 Br. 9), and that the "record fails to reflect whether the Tax Court modified or reversed its trial judge's findings" (03-1034 Br. 38). Equally baseless is the claim (03-1034 Br. 1) that the government has conceded that the STJ's findings were "revers[ed]" by the Tax Court judge. The government has consistently argued that the statement by STJ Couvillion, Judge Dawson and Chief Judge Wells refutes that contention. See 03-1034 Resp. Br. in Opp. 12; 03-184 Resp. Br. in Opp. 13 & n.3.

B. Petitioners' Claims Thus Reduce To An Impermissible Attempt To Compel Disclosure Of The Tax Court's Internal Deliberative Processes

Petitioners' request for the "original STJ report" thus boils down to a claim for any initial report that the STJ submitted to the Chief Judge of the Tax Court but later abandoned in favor of the "final" report published in the record. That request should be refused by this Court. Even assuming that such an "original" report was submitted by STJ Couvillion, that report would reflect, not his ultimate decision, but a step in his confidential decisional process.

It is well settled that litigants are not entitled to compel disclosure of a judge's or agency's pre-decisional deliberative process. *See, e.g., Fayerweather* v. *Ritch*, 195 U.S. 276, 306-308 (1904); *Chicago, Burlington & Quincy Ry.* v. *Babcock*, 204 U.S. 585, 593 (1907). See also *In re Cook*, 49 F.3d 263, 265-266 (7th Cir. 1995) ("federal judges speak through their opinions"; "[i]nquiry beneath the surface of a judge's opinion is forbidden"); *Goetz* v. *Crosson*, 41 F.3d 800, 805 (2d Cir. 1994), cert. denied, 516 U.S. 821 (1995) ("[t]he inner workings of administrative decision making processes are almost never subject to discovery. * * * Clearly, the inner workings of decision making by courts are kept in even greater confidence."); *United States* v. *Crouch*, 566 F.2d 1311, 1316 (5th Cir. 1978) (same).

This Court reaffirmed that principle in *United States* v. *Morgan*, 313 U.S. 409, 417-422 (1941) (*Morgan IV*), which involved a challenge to a rate determination by the Secretary of Agriculture. In the district court, the Secretary had been deposed and made to explain "the process by which he reached the conclusions of his order" so that the court could evaluate whether the Secretary had conducted a fair hearing. *Id.* at 422. In affirming the Secretary's determination, this Court held that "the Secretary should never have been subjected to this examination." *Ibid.* The Court explained,

"it [is] not the function of the court to probe the mental processes" of administrative or judicial decisional authorities. *Ibid.* Rather, "[s]uch an examination of a judge would be destructive of judicial responsibility. * * * Just as a judge cannot be subjected to such a scrutiny, so the integrity of the administrative process must be equally respected." *Ibid.* (internal citations omitted).

Petitioners' suggestion (03-184 Br. 35-43) that STJ Couvillion's deliberative process should nonetheless be disclosed to determine whether his findings were coerced by or the result of improper collaboration with Judge Dawson represents an impermissible intrusion into the court's decision-making process.

1. Petitioners' Claim Of Improper Influence On STJ Couvillion Lacks Factual Support

Petitioners' allegation of improper influence on STJ Couvillion rests on the uniform acceptance of STJ reports by Tax Court judges (03-1034 Br. 8-10, 15-16, 21; 03-184 Br. 7-10, 16-17, 19 & n.14), a hearsay affidavit from petitioners' counsel about alleged "revisions" to STJ Couvillion's report (03-1034 Br. 6a), and surmise (03-184 Br. 9, 41-42) premised on the STJ hiring process. None of those assertions provides a sufficient basis for requiring disclosure of the Tax Court's internal deliberative process.

The tendency of STJs and Tax Court judges to agree is not probative of improper influence. Such agreement was evident prior to 1983, when under then-Tax Court Rule 182, STJ reports were served on the parties, who could then file exceptions. See Tax Ct. R. 182(b) (1974). From 1976 to 1983, for example, there were only *six* cases, out of approximately 680 decisions, in which the Tax Court did not adopt the opinion of the STJ, and only *one* case in which the Tax Court

"reversed" the STJ.[4] Thus, even when the STJ's report was available to the parties prior to the Tax Court's review, full adoption of STJ recommendations was the rule, not the exception.

The Declaration of Randall G. Dick (03-1034 Br. App. 5a-7a) also fails to demonstrate misconduct. It states only that petitioners' counsel heard that "changes to judge Couvillion's findings relating to credibility and fraud were made by Judge Dawson" in a way that constituted an "outright

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[4] See *Kansas City S. Ry.* v. *Commissioner*, 76 T.C. 1067 (1981); *Narver* v. *Commissioner*, 75 T.C. 53 (1980); *Hilton* v. *Commissioner*, 74 T.C. 305 (1980); *La Fargue* v. *Commissioner*, 73 T.C. 40 (1979); *C. Blake McDowell, Inc.* v. *Commissioner*, 67 T.C. 1043 (1977), vacated and remanded, 576 F.2d 718 (6th Cir.), on remand, 71 T.C. 71 (1978), aff'd, 652 F.2d 606 (6th Cir. 1980). In 14 (out of approximately 680) other cases, the Tax Court adopted the opinion of the STJ with modifications that were, in most instances, described as "minor." See *Ocean Sands Holding Corp.* v. *Commissioner*, 41 T.C.M. (CCH) 1, 2 (1980) ("minor modifications"), aff'd, 701 F.2d 163 (4th Cir.) (Table), cert. denied, 464 U.S. 827 (1983); *Taylor* v. *Commissioner*, 41 T.C.M. (CCH) 539, 539 (1980) ("some modifications"); *Perrett* v. *Commissioner*, 74 T.C. 111, 111 (1980) ("minor modifications"), aff'd, 679 F.2d 900 (9th Cir. 1982) (Table); *Karme* v. *Commissioner*, 73 T.C.M. 1163, 1163 (1980) ("minor modifications"), aff'd, 673 F.2d 1062 (9th Cir. 1982); *Freidus* v. *Commissioner*, 39 T.C.M. (CCH) 740, 740, (1979) ("some amendments"); *McKinley* v. *Commissioner*, 37 T.C.M. (CCH) 1769, 1769 (1978) ("minor modifications"); *Estate of Thurner* v. *Commissioner*, 37 T.C.M. (CCH) 981, 982 (1978) ("modified in minor respects"); *Ward* v. *Commissioner*, 37 T.C.M. (CCH) 928, 928 (1978) ("minor changes"); *Dante* v. *Commissioner*, 37 T.C.M. (CCH) 556, 556 (1978) ("minor modifications"); *Estate of Marcello* v. *Commissioner*, 36 T.C.M. (CCH) 1408, 1409 (1977) ("minor changes"); *Jacqueline, Inc.* v. *Commissioner*, 36 T.C.M. (CCH) 1363, 1363 (1977) ("[s]ome modifications"), modified, 37 T.C.M. (CCH) 937 (1978); *Ducar* v. *Commissioner*, 36 T.C.M. (CCH) 1278, 1279 (1977) ("minor changes"); *Graham* v. *Commissioner*, 35 T.C.M. (CCH) 1315, 1316 (1976) ("minor modifications"); *Louisville & Nashville R.R.* v. *Commissioner*, 66 T.C. 962, 963 (1976) ("some amendments"), aff'd in part, rev'd in part and remanded, 641 F.2d 435 (6th Cir. 1981).

rejection of credibility findings" initially proposed by the STJ. *Id.* at 6a. Even assuming arguendo the truth of those hearsay statements, whether Judge Dawson suggested "revisions" is of no moment so long as STJ Couvillion ultimately agreed with and adopted those changes in his report. The order signed by, *inter alia*, STJ Couvillion should end any speculation about whether his report might have been "revised" without his consent, because it flatly states that his report was adopted by Judge Dawson. 03-184 Pet. App. 315a.

Finally, petitioners cannot raise the specter of impropriety by claiming that STJs are hired and fired by regular Tax Court judges (03-184 Br. 9, 41-42). STJs *cannot* be hired or fired by the regular judges to whom they report, but are salaried, full-time employees appointed solely by the Chief Judge. See 26 U.S.C. 7443A(a); Tax Ct. R. 180. There is nothing in the record, or indeed the entire history of the Tax Court, to suggest that STJ Couvillion (or any other STJ) has ever been threatened with termination or otherwise improperly coerced into adopting a view of the case advanced by the regular Tax Court judge but contrary to his own views. Nor is there any basis for concluding that any STJ would acquiesce in the face of such conduct.

2. As A Matter Of Law, Judicial Misconduct Will Not Be Presumed

Beyond those factual deficiencies, petitioners' suggestion of misconduct in the Tax Court's deliberative process is legally flawed for two reasons. First, petitioners' attempt to require disclosure of the Tax Court's internal deliberative process in order to *discover* whether any improprieties have occurred turns the standard assumption about judicial conduct on its head. Courts should not be "inclined to assume" nefarious conduct on the part of judges, but should accept a judge's claim that he has performed his judicial responsibilities absent "proof" by a challenging party to the contrary.

Freytag v. *Commissioner*, 501 U.S. 868, 872 n.2 (1991). Cf. *Erhard* v. *Commissioner*, 46 F.3d 1470, 1476 (9th Cir. 1995); *Richardson* v. *Town of Eastover*, 922 F.2d 1152, 1161 (4th Cir. 1991). Thus, where a judge denies the factual basis for a recusal claim, the denial ends the matter. *E.g.*, *Sao Paulo State of Federative Republic of Brazil* v. *American Tobacco Co.*, 535 U.S. 229, 233 (2002) (crediting judge's rendition); *In re Brooks*, No. 03-5047, 2004 WL 2032521, at *6 (D.C. Cir. Sept. 14, 2004) (same). Similarly, where a judge's partiality is questioned, the claim is examined "in light of the facts" set forth in the judge's report, "and not as they were surmised or reported" erroneously by those not present. *Cheney* v. *U.S. Dist. Court*, 124 S. Ct. 1391, 1392 (2004) (Scalia, J.).

Accordingly, the proper starting point in this case is the order signed by STJ Couvillion, Judge Dawson and the Chief Judge Wells. That order states that Judge Dawson "adopted the findings of fact and opinion of Special Trial Judge Couvillion" and gave "due regard" to the STJ's recommendations. 03-1034 Pet. App. 102a; 03-184 Pet. App. 315a. If those statements were incorrect, the STJ would "say so," and neither he nor Chief Judge Wells nor Judge Dawson would have signed the order. 03-1034 Pet. App. 13a. For the same reason, the numerous Tax Court opinions that, like the decision below, begin "the Court agrees with and adopts the opinion of the Special Trial Judge, which is set forth below," should be taken at face value.

Second, to the extent petitioners' claim is merely that STJs and Tax Court judges collaborate in a way that allows a Tax Court judge to influence an STJ recommendation before the STJ finalizes it, their claim lacks legal merit. There is simply no legal prohibition against judges exchanging ideas, or even vigorously lobbying one another, in an attempt to influence the decision-making process. To the contrary, judges routinely "confer[] with one another about cases assigned to them," and sometimes change their minds about

a case as a result of those consultations. 03-1034 Pet. App. 13a-14a. Because "votes are not final until decisions are final; and decisions do not become final until they are released, accompanied by an explanation of the reasons for the result," the mere fact that "the exchange of draft opinions can and does change votes" does not violate due process. *Checkosky* v. *SEC*, 23 F.3d 452, 489-490 (D.C. Cir. 1994). While that kind of back and forth between judges is most familiar in the context of judges jointly hearing a case as a panel, nothing precludes such interchange between the STJ and a Tax Court judge in light of the particular structure of decisionmaking reflected in Rule 183. See pp. 24-29, *infra*.

The exchange of drafts and ideas between an STJ and a regular judge of the Tax Court similarly is not forbidden "ex parte" communication. See 03-184 Br. 9-10, 36-40. Indeed, the assertion is wrong by definition, because neither the Tax Court judge nor the STJ is a "party" in the case. See *Black's Law Dictionary* 597 (7th ed. 1999) (defining "ex parte" as "[d]one or made at the instance and for the benefit of one party only"). To be sure, where different employees of an agency perform investigatory, prosecutorial, and adjudicative responsibilities, those employees with investigative and prosecutorial duties will generally not have a role in the adjudicative process. See 5 U.S.C. 554(d)(2); *Morgan* v. *United States*, 304 U.S. 1, 19-20 (1938) (*Morgan II*). Tellingly, however, there is no such prohibition against confidential communications between an agency head, who serves as the final agency adjudicator, and a hearing examiner regarding a pending adjudicative matter. Congress expressly *exempted* such communications from the prohibition against prosecutorial contacts. 5 U.S.C. 554(d)(2)(C).

This Court acknowledged the practice of confidential communication between decisional authorities and hearing officers in *Morgan IV*. The parties challenging the Secretary of Agriculture's rate determination in that case

asserted *inter alia* that "the Secretary * * * conferred on several different occasions with the Examiner concerning the evidence and the findings to be made thereon out of the presence of appellee market agencies and their counsel," that the Examiner was "an employee dominated by the Secretary," and that the Secretary effectively "told the Trial Examiner which way the Secretary would like the case to go upon the merits." Br. for Appellees at 58, 109, 113, *United States* v. *Morgan*, 313 U.S. 409 (1941) (No. 640). The Court likewise noted that the Secretary had "held various conferences with the examiner who heard the evidence" (313 U.S. at 422), but stated that he had "dealt with the enormous record in a manner not unlike the practice of judges in similar situations." *Ibid.* The Court upheld the Secretary's decision, concluding that "[t]he record leaves no doubt that the Secretary * * * appropriately discharged [his] duty." *Id.* at 415.

3. Disclosure Of An "Original" Report Could Not Benefit Petitioners Absent Further Unacceptable Intrusions Into The Tax Court's Deliberative Process

Allowing petitioners to obtain access to an "original," but subsequently abandoned, STJ report would lead only to more demands for intrusion into the Tax Court's deliberative process. Mere disclosure of such an original report could not in itself provide any basis for granting petitioners relief from the judgment of the Tax Court, because the record is clear that STJ Couvillion's final recommendations regarding the disposition of this case are embodied *in toto* in the decision of the Tax Court. The Tax Court judge did not reverse, modify, or set aside those recommendations, and thus there would be nothing of relevance to be considered by the courts of appeals even if petitioners could establish that the STJ changed his views over the course of the deliberative process. That a judge changed his mind before adopting his

final view of a case is hardly grounds for setting aside a final judgment. Indeed, the courts below have *already held* that proof of such a change of mind would not invalidate the Tax Court's judgment; the mere disclosure of any abandoned "original" report would thus avail petitioners nothing. 03-184 Pet. App. 9a-10a ("Whether Special Trial Judge Couvillion prepared drafts of his report or subsequently changed his opinion is entirely without import."); 03-1034 Pet. App. 13a ("Any differing preliminary recommendations—if they ever existed—would no longer be constitutionally relevant because the STJ has abandoned them.").

In order to have any prospect of obtaining relief from the judgment of the Tax Court, therefore, petitioners could not be content with the mere disclosure of an "original" report. Instead, petitioners would have to pursue still further discovery in an effort to identify some evidentiary basis for their allegations that STJ Couvillion did not in fact agree with the findings set forth as his report in the decision of the Tax Court. In short, petitioners would need to reconstruct the entire internal deliberative process, presumably by requests to depose STJ Couvillion and Judge Dawson.

Far from being a requirement of due process, subjecting judges to examination to learn about their decisional process has never been countenanced by this Court. See *Morgan IV*, 313 U.S. at 422; *Fayerweather*, 195 U.S. at 306-307. The first step toward that examination should not be taken here. Petitioners' claims should be rejected—or the writs of certiorari should be dismissed as improvidently granted—because even a ruling in petitioners' favor on the questions presented could not change the final disposition below in the absence of still further, and patently impermissible, discovery of the Tax Court's internal deliberations.

II. THE TAX COURT'S PROCEDURES COMPORT WITH DUE PROCESS

Petitioners contend that non-disclosure of an "original" STJ report precludes effective appellate review, departs from historical and contemporary judicial practice in violation of due process, and violates *Mathews* v. *Eldridge*. Even if presented by this case, those arguments would lack merit.

A. Disclosure Of An "Original" STJ Report Is Unnecessary For Effective Appellate Review

Petitioners' arguments concerning effective appellate review assume that an STJ functions as a trial court judge whose factual recommendations must be accepted absent "clear error." Thus, petitioners claim, STJ reports must be disclosed so that the courts of appeals can consider whether the Tax Court properly applied the "clearly erroneous" standard of review in rejecting any findings recommended by the STJ. That argument fundamentally misunderstands the function and responsibilities of STJs.

1. The Tax Court Judge, Not The STJ, Determines Facts And Legal Conclusions

In cases such as this, tried pursuant to Section 7443A(b)(4) of the Internal Revenue Code, STJs are simply not authorized to function as trial court judges whose findings are reviewable only for clear error. By statute, STJs are precluded from entering the "decision of the Tax Court" as to either fact or law in proceedings of the type at issue here. See 26 U.S.C. 7443A(c). In *Freytag* v. *Commissioner*, 501 U.S. 868, 873-876 (1991), this Court settled the question, holding that STJs "ha[ve] no authority to decide a case assigned [to them] under subsection (b)(4)" of Section 7443A. *Id.* at 875 n.3. The "authority actually to decide those cases * * * is reserved *exclusively* for judges of the Tax Court." *Id.* at 874 (emphasis added).

Consistent with that statutory mandate, the Tax Court's rules confer decisional authority only on the regular judge of the Tax Court when a case is heard by an STJ under Section 7443A(b)(4). Rule 183(c) provides that the judge "may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may recommit the report with instructions." Tax Ct. R. 183(c); see 26 U.S.C. 7443A(c). Thus, the only decision relevant for appellate review is the decision of the Tax Court. 26 U.S.C. 7443A(c), 7460(b); see 03-1034 Pet. App. 8a ("The Tax Court thus acts as the original finder of fact.").

2. The Tax Court Is Not Required By Its Rules To Review STJ Reports For Clear Error

Petitioners' contrary argument (e.g. 03-184 Br. 22-23, 31-32; 03-1034 Br. 4-5, 17-18, 19-20) derives from their misreading of Tax Court Rule 183(c) to require review of STJ reports under the "clear error" standard or a similarly deferential standard of review. As explained in Part I above, the standard-of-review issue is not presented in this case, because the record demonstrates that the Tax Court judge did not reverse or set aside, but instead accepted, the STJ's recommended findings. In any event, petitioners are mistaken; far from requiring clear-error review, current Tax Court Rule 183 eliminated any sort of appellate-style review from proceedings within the Tax Court.

The current Tax Court Rule 183(c), which was adopted in 1983, provides:

> The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral argument, or may

> recommit the report with instructions. Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct.

Tax Ct. R. 183(c). In contrast, Rule 183's predecessor, Rule 182, had (since 1974) contained similar language concerning "due regard" and the presumed correctness of STJ reports, but also required STJs to "serve[]" their reports, "including" any "findings of fact and opinion," on the parties and provide the parties an opportunity to file briefs with the Tax Court setting forth their "exceptions" to the report, and to request argument on the issues so briefed. Tax Ct. R. 182(a), (b), (c) and (d) (1974). In 1983, the Tax Court amended the rule to its current form, "delet[ing]" "[t]he prior provisions for service of the Special Trial Judge's report on each party and for the filing of exceptions to that report." Tax Ct. R. 183 note (1984).

By altering its rules specifically to *eliminate* disclosure of and exceptions to STJ reports, the Tax Court has made plain that it does not contemplate any sort of appellate-style review of STJ reports. See *Freytag* v. *Commissioner*, 904 F.2d 1011, 1015 n.8 (5th Cir. 1990) (observing that rule change "confirm[ed] that the Tax Court's relationship with its special trial judges cannot be analogized to typical appellate review"), aff'd, 501 U.S. 868 (1991). Although Rule 183(c) continues to instruct Tax Court judges to give "due regard" to the "circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses," and "presume[]" STJ findings "to be correct," that language does not require review of STJ reports for clear error. Instead, it merely requires Tax Court judges "to be cognizant that the STJ had the opportunity to evaluate the credibility of witnesses." 03-1034 Pet. App. 8a. On this point, even the sole dissenting judge in the proceedings below

agreed. *Id.* at 75a (Cudahy, J., concurring in part and dissenting in part) ("Rule 183 imposes no requirement of disclosure or of clearly erroneous deference upon the Tax Court").

Ascribing a deeper meaning to the "due regard" and "presumed to be correct" language would not comport with the Tax Court note explaining the addition of that language in 1974. The note provides that the amendment was intended to *expand* the decisional authority of Tax Court judges with respect to STJ reports, stating that "[t]he decision of a case is made by a Judge, and the rule *expands* the alternatives available in reviewing the determinations of the commissioner as embodied in his report. The Judge, to whom the case is assigned, may take *any* action he deems appropriate for a proper disposition of the case, *even with respect to the commissioner's findings of fact*, although they are accorded special weight insofar as those findings are determined by the opportunity to hear and observe the witnesses." Tax Ct. R. 182(b) note (1974) (emphasis added).[5] Thus, notwithstanding the "due regard" and "presumed correct" language, the Tax Court intended to retain full decisional authority over cases under the new rule.

The Tax Court's own interpretation of its procedures bolsters that reading of Rule 183. In *Rosenbaum* v. *Commissioner*, 45 T.C.M. (CCH) 825, 827 (1983), the Tax Court was asked to consider whether it had given the deference required under former Rule 182 to an STJ report. The court

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[5] Petitioners argue (03-1034 Br. 31) that a reference in this note to "Court of Claims procedures" demonstrates the Tax Court's intent to review reports for clear error, as that was the existing practice of the Court of Claims when former Rule 182 was adopted. But the note, by its terms, does not suggest an intent to *duplicate* the Court of Claims' standards of review; it provides only that the Tax Court's procedures should be "*more comparable* to those which obtain in the Court of Claims." Tax Ct. R. 182 note (emphasis added).

observed that while its rules required it to give "due regard to the circumstance that the Special Trial Judge had the opportunity to see and evaluate the credibility of witnesses," "the presumptive correctness of the Special Trial Judge's report does not impair nor dilute our duty of bearing the ultimate responsibility for determining matters before us." *Ibid.*

Petitioners' reliance on *Stone* v. *Commissioner*, 865 F.2d 342 (D.C. Cir. 1989), rev'g *sub nom. Rosenbaum* v. *Commissioner*, 45 T.C.M. (CCH) 825, 827 (1983) (03-1034 Br. 7 n.2, 28-34; 03-184 Br. 17, 22, 27-28), for a contrary interpretation of the "due regard" language is misplaced.[6] In *Stone*, the D.C. Circuit held that the Tax Court was required under former Tax Court Rule 182 to review the recommended findings of STJs under a clearly erroneous standard. 865 F.2d at 345-347.

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[6] Kanter errs in asserting (Br. 32) that the government has conceded the validity of the *Stone* decision. The government has long regarded *Stone* as wrongly decided in light of the D.C. Circuit's failure to defer to the Tax Court's interpretation of its own rule. See Resp. Br. at 19 n.10, *Freytag* v. *Commissioner*, *supra*. Indeed, shortly after *Stone* was decided, the government explained its view of the case as follows:

> the Tax Court has never retreated from the position it took in *Rosenbaum* that "the presumptive correctness of the Special Trial Judge's report does not impair nor dilute our duty of bearing the ultimate responsibility for determining matters before us." *Rosenbaum*, 45 T.C.M. (CCH) at 827. In accordance with that position, the Tax Court no longer furnishes litigants a copy of the special trial judge's report, nor does it invite the parties to file exceptions to the report. *Ibid.*; Pet. App. A8 n.8. As the court of appeals concluded, "this change in rules, in our view, confirms that the Tax Court's relationship with its special trial judges cannot be analogized to typical appellate review." *Ibid.* No court has held to the contrary since the change in the Tax Court's practice.

Ibid.

Given that *Stone* was decided under former Rule 182, which contained the service-and-objection requirement, it is inapposite here. By eliminating the service-and-objection procedures, the Tax Court has removed any ambiguity over whether STJs function like trial court judges subject to appellate-style review by Tax Court judges. *Freytag*, 904 F.2d at 1015 n.8. Thus, those courts considering the validity of *Stone* since the Tax Court adopted Rule 183(c) have uniformly concluded that it does not mandate review of STJ findings by the Tax Court for clear error. See *ibid.*; 03-1034 Pet. App. 8a-9a ("The Tax Court thus acts as the original finder of fact. * * * [T]he STJ's inability to decide cases limits the amount of deference that the Tax Court, as the original factfinder, must pay to those preliminary findings."); *id.* at 75a (Cudahy, J., concurring in part, dissenting in part) ("Rule 183 imposes no requirement of disclosure or of clearly erroneous deference upon the Tax Court."); accord *Estate of Lisle* v. *Commissioner*, 341 F.3d 364, 384 (5th Cir. 2003).[7]

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[7] Even if the Court were to conclude that the 1983 amendment to Rule 183 is problematic because of tension between the non-disclosure rule and the "due regard" and "presumed to be correct" language, the proper remedy would not be to compel disclosure of "original" STJ reports. The Tax Court eliminated the practice of disclosing STJ reports, and the "due regard" and "presumed to be correct" language can be construed as internal direction to guide the Tax Court judges in considering STJ reports. But if that language were inherently to give rise to rights in the taxpayer, that language should give way to the Tax Court's clear intent to eliminate disclosure and briefing. Nothing in the Constitution or the Internal Revenue Code required the Tax Court to retain the provisions regarding deference to STJ recommendations. Thus, if the Tax Court's failure to delete the "due regard" and presumption language in 1983 cannot be reconciled with the court's non-disclosure rule, the proper result would be to invalidate the offending language in the rule, not to reject the Tax Court's clear policy decision to preserve the confidentiality of initial STJ reports. At the very least, a remand to the Tax Court would be required to permit that court to decide the question of severability that would be raised in those circumstances. Cf. *Davis* v. *Michigan Dep't of Treasury*,

B. The Tax Court's Practice Is Neither Unprecedented Nor Unjustified

Petitioners contend (03-1034 Br. 17, 23-24; 03-184 Br. 17, 43- 46) that disclosure of initial STJ reports is required by virtue of historical and contemporary judicial and administrative practice. *Ibid.* (citing *Honda Motor Co.* v. *Oberg*, 512 U.S. 415, 430 (1994)). Those contentions are incorrect.

As an initial matter, petitioners overlook the well-established principle that the procedures followed in the Article III context generally do not define the proper benchmark for evaluating tax proceedings, because such proceedings do not require the full complement of procedural safeguards that may be necessary elsewhere. At common law, tax cases were resolved in a branch of the "court of exchequer" and were not "judicial controversies * * * according to the ordinary course of the common law or equity." *Murray's Lessee* v. *Hoboken Land & Improvement Co.*, 59 U.S. (18 How.) 272, 282 (1855). The Exchequer was a "department" in which "a court of revenue [was] held before the Treasurer," and which was "probably the nearest approach to a body of administrative law that the English legal system has ever known; and the court of Exchequer, sitting as a court of Revenue, is the nearest approach to an administrative court." 1 W. Holdsworth, *A History of English Law* 231, 238, 239 (1926). See A. Carter, *A History of the English Courts* 51 (7th ed. 1944).

Indeed, this Court has concluded that tax cases are "public rights" cases, which "congress may or may not bring within the cognizance of the courts of the United States, as it may deem proper." *Crowell* v. *Benson*, 285 U.S. 22, 50 (1932) (quoting *Murray's Lessee*, 59 U.S. (18 How.) at 284); *Northern Pipeline Constr. Co.* v. *Marathon Pipe Line Co.*,

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489 U.S. 803, 818 (1989); *Atchison, Topeka & Santa Fe Ry.* v. *Wichita Bd. of Trade*, 412 U.S. 800, 822 (1973).

458 U.S. 50, 68, 70 n.23 (1982) (as to matters involving "public rights," a category of cases that includes "taxation," Congress "would be free to commit such matters completely to nonjudicial executive determination"); *Ex parte Bakelite Corp.*, 279 U.S. 438, 451 (1929). Accordingly, it has long been recognized that tax disputes may be subject to unique procedures that might otherwise be impermissible in the Article III context. See *Murray's Lessee*, 59 U.S. (18 How.) at 284. That principle follows from the fact that "the very existence of government depends upon the prompt collection of the revenues." *G. M. Leasing Corp.* v. *United States*, 429 U.S. 338, 352 n.18 (1977).

In any event, petitioners are wrong in characterizing the Tax Court's practice as unique or aberrational. Most saliently, there is a direct *statutory* analog to the Tax Court's STJ practice: the non-disclosure of a regular Tax Court judge's opinion when a case is reviewed by the full Tax Court. From the earliest days of the Tax Court's predecessor, Congress has provided that initial reports reflecting the proposed disposition of a case were subject to review by the full court, and when that option is exercised Congress has *required* the exclusion of the "original" report from the record. See Revenue Act of 1928, ch. 852, § 601, 45 Stat. 871. That historical practice continues today with Section 7460(b) of the Internal Revenue Code, which directs that, in cases of full court review, the report of the regular judge "shall not be a part of the record." 26 U.S.C. 7460(b); see *Estate of Varian* v. *Commissioner*, 396 F.2d 753, 754-755 (9th Cir.) (rejecting argument that due process requires inclusion of the regular judge's opinion in the record), cert. denied, 393 U.S. 962 (1968); *Heim* v. *Commissioner*, 251 F.2d 44, 45-46 (8th Cir. 1958) (same).

Outside the tax context, the numerous boards of contract appeals established by various agencies similarly do not require disclosure of initial reports prepared by presiding

judges and submitted to other judges for final decision. Under the Contract Disputes Act, 41 U.S.C. 601 *et seq.*, administrative agencies are authorized to establish boards of contract appeals to resolve certain contract disputes between the agency and contractors. See 41 U.S.C. 607. Such boards are typically comprised of a chairperson and several administrative judges. The chairperson typically assigns a case to a panel of administrative judges, one of whom is designated the "presiding judge" responsible for conducting any evidentiary hearing. The presiding judge's initial proposed decision and credibility assessments are not disclosed to the parties or reviewed only for clear error by the other panel members. Only the panel's final decision is served on the parties and included in the record.[8] As with STJ reports, the recommendations of a presiding judge who hears the evidence firsthand can be rejected by the other judges on the panel, who review only the record and the presiding judge's proposed disposition. *E.g. Lockheed Martin Tactical Def. Sys., Inc.*, Contract No. N00039-86-C-0452, 2000 WL 626879, at n.1 (Armed Serv. Bd. Cont. App. May 3, 2000) (rejecting credibility assessments of presiding judge); *Appeal of Ash Anlagen-Und Sanierungstechnik GMBH*, Contract No. DAJA76-87-C-0467, 2003 WL 22230677 (Armed Serv. Bd. Cont. App. Sept. 24, 2003) (same); *Smith & Oby Co.* v. *General Servs. Admin.*, No. 15336, 2003 WL 22100648 (Gen. Servs. Admin. Bd. Cont. App. Sept. 5, 2003) (retirement of presiding judge prior to decision). That system of non-disclosure and non-deference to the hearing officer's

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[8] *E.g.*, Gen. Servs. Admin. Bd. Cont. App. R. 101(e) ("Each case will be assigned to a panel consisting of three judges, with one member designated as the panel chairman. * * * The panel chairman is responsible for processing the case, including scheduling and conducting proceedings and hearings."), 122(c) (the "Board" determines "the credibility to be accorded to witnesses"), 129 (parties provided with only decision of board). See also 7 C.F.R. 24.2, 24.3, 24.21; 38 C.F.R. 1.781, 1.783.

recommendations is accepted practice because the full panel, not the presiding judge, is understood to render decision. See *Bill J. Copeland*, No. 2003-124-R, 2003 WL 1740503 (Dep't of Agriculture Bd. Cont. App. Feb. 20, 2003) (rejecting request for rehearing after retirement of presiding judge on the ground that "[a] presiding judge has no greater say in the outcome of an appeal than the other members"); *Charles G. Williams Constr.* v. *White*, 326 F.3d 1376, 1381 (Fed. Cir. 2003) (rejecting argument that presiding judge is "particularly well qualified" to evaluate credibility as sole officer hearing witnesses).

The counter-examples offered by petitioners (03-1034 Br. 23- 24; 03-184 Br. 39-40), such as the procedures governing ALJs and magistrate judges, are inapposite. In the first place, that Congress has chosen to mandate disclosure of initial recommended decisions in those contexts is no basis for extending the same requirement to other settings. By expressly precluding disclosure of "reviewed" decisions of Tax Court judges (26 U.S.C. 7460(b)), Congress has signaled that it sees no constitutional objections to proceeding in that manner. In the same way, by granting exclusive rulemaking authority to the Tax Court (26 U.S.C. 7443A(a), 7453), Congress has empowered that court, at a minimum, to choose between the two ways of treating initial opinions that Congress has found advisable in different contexts.

Petitioners' examples are, in any event, inapt. By statute, an ALJ's recommended decision *automatically* "becomes the decision of the agency" unless a party objects, without any review whatsoever by the ultimate agency decisionmaker. 5 U.S.C. 557(b).[9] Given that fact, it is unsurprising that Con-

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[9] Unless a party interposes an objection, the factual recommendations of a magistrate judge can automatically be made the findings of the court without further review by the district judge. See 28 U.S.C. 636(b)(1)(A); *Thomas* v. *Arn*, 474 U.S. 140, 148-152 (1985); see also Fed. R. Civ. P. 53(g)(3) (special masters); *Kentucky* v. *Indiana*, 474 U.S. 1, 1 (1985) ("The

gress has required that ALJ decisions be disclosed, thereby giving parties the opportunity to invoke review by the final agency decisionmaker. See 5 U.S.C. 557(c). STJ reports do not operate in the same manner, because Congress has statutorily *precluded* STJs from functioning as decisionmakers in this context. See 26 U.S.C. 7443A(b)(4) and (c); *Freytag*, 501 U.S. at 875 n.3.[10]

Even if the Tax Court's practices lacked historical pedigree or modern analog, they would not be unconstitutional simply by virtue of their supposed novelty. Courts often adopt procedures without historical precedent to respond to the unique demands of the day, such as class action suits, multi-district litigation, and even the merger of courts of equity and courts of law. The Tax Court itself is a relatively modern innovation that responded to the perceived need for a tribunal in which taxpayers could quickly and easily settle their disputes before paying a disputed tax. The Tax Court's practices are a reflection of its special role as an informal, nationwide tribunal for the efficient resolution of taxpayer claims.

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parties having waived the right to file Exceptions, the Report [of the Special Master] is adopted."). In any event, the magistrate and special-master examples are inapposite because they arise in the Article III context, where the Constitution imposes constraints on the utilization of adjunct decisionmakers.

[10] Petitioners' reliance on *Universal Camera Corp.* v. *NLRB*, 340 U.S. 474, 493 (1951), for the proposition that disclosure of a hearing examiner's report is necessary "to accurate appellate adjudication" (03-1034 Br. 35; see 03-184 Br. 25) is misplaced. The statutes at issue in *Universal Camera* required that the hearing examiner include his report in the record, and "the plain language of the statutes direct[ed] a reviewing court to determine the substantiality of evidence on the record including the examiner's report." *Universal Camera*, 340 U.S. at 493 (citing the Taft-Hartley Act, ch. 120, § 10(c), 61 Stat. 148, and the Administrative Procedure Act, ch. 324, § 8(b), 60 Stat. 242; see 5 U.S.C. 557(c)). No such statutes apply here.

As one commentator on Rule 183(c) has observed, the Tax Court is unique in that it is a single nationwide court that "speaks with a single voice" while expeditiously resolving cases among 19 judges who still ride circuit. A. Madison, *Revisiting Access to the Tax Court's Deliberative Process*, Tax Notes, May 10, 2004, at 751. Imposing an appellate-style review process on the court would add an unnecessary layer of decision to the detriment of the quick and easy resolution of Tax Court proceedings. *Ibid.*

Indeed, while the Tax Court did not set forth its rationale for amending its rules in 1984 to preserve the confidentiality of STJ reports, the events of the time strongly suggest that the amendment was necessary to the expeditious resolution of cases. Congress made major revisions to the Internal Revenue Code that increased taxpayer liability for abusive tax shelters, and in early 1983, then-Tax Court Chief Judge Designate Tannenwald warned that he "anticipated increases in the number of shelter and tax protester cases * * * from the newly enacted provisions of the Internal Revenue Code." *Treasury, Postal Service, and General Government Appropriations for Fiscal Year 1984: Hearings Before the Subcomm. of the House Comm. on Appropriations*, 98th Cong., 1st Sess. Pt. 4, at 8 (1983) (FY 1984 Hearings). In fact, the Tax Court was quickly flooded with tax shelter petitions; the number of cases filed with the court doubled from 1980 to 1985, increasing nearly 50% from fiscal years 1982 to 1985 alone. See *Treasury, Postal Service, and General Government Appropriations for Fiscal Year 1987: Hearings Before the Subcomm. of the House Comm. on Appropriations*, 99th Cong., 2d Sess. Pt. 4, at 355, 380 (1986). The court's backlog of pending cases increased at a similar rate: between fiscal years 1982 and 1985, the number of authorized Tax Court judges remained steady at 19, while the number of pending cases increased by more than 38%. *Id.* at 361; see FY 1984 Hearings at 49; 26 U.S.C. 7443.

Faced with that anticipated flood of litigation, the Tax Court removed the disclosure and objection provisions when it promulgated Rule 183, and eliminated the unnecessary layer of additional briefing and argument the court had previously permitted.

This reading of history is supported by a similar amendment to the Tax Court's rules that occurred only a few years before the disclosure provisions were eliminated entirely in 1984. In 1976, the Tax Court eliminated the service-and-objection requirement in STJ cases that did not fall within the court's "small tax case" docket but involved amounts under $2500, at a time when it was facing a surge in such cases. The court explained that the increasing "number of new cases filed in the United States Tax Court * * * involving deficiencies under $2,500" required it "to make changes in the present practices of the Court in order to dispose of pending cases more promptly and efficiently." Tax Ct. General Order No. 5, at 1 (Oct. 1, 1976). To that end, in all such cases the court permitted STJs to submit a report for decision directly to the Chief Judge of the Tax Court, without disclosure of the report to the parties and without an opportunity for the parties to object to the report. *Id.* at 1-2. In the court's view, it was "clearly impracticable and undesirable to follow the post-trial procedures" regarding STJ reports in those cases. *Id.* at 2. It is reasonable to infer that the Tax Court was motivated by the same logic when it eliminated the same procedures from the remaining cases tried before STJs a few years later.

C. Deference To An STJ's Credibility Determinations Is Not Constitutionally Compelled

Contrary to petitioners' claim (03-184 Br. 17-19, 29-34, 36, 40-41; 03-1034 Br. 38), disclosure of the STJ's initial credibility assessments is not necessary to prevent the Tax Court from rejecting them "without seeing and hearing the wit-

ness" in violation of *United States* v. *Raddatz*, 447 U.S. 667, 681 n.7 (1980).

At the outset, even if Tax Court judges were engaged in such a practice, it would raise no constitutional concern here. The suggestion in *Raddatz* that a judge's rejection of a magistrate's credibility determinations without hearing the witnesses "could well give rise to serious questions" was made in the context of a *criminal* proceeding, 447 U.S. at 681 n.7, which requires an Article III forum and a higher level of procedural protection than is required in civil tax cases. See *Moyer* v. *Peabody*, 212 U.S. 78, 84 (1909) ("[D]ue process of law depends on circumstances. * * * Thus summary proceedings suffice for taxes, and executive decisions for exclusion from the country.") (citing *Murray's Lessee*, 59 U.S. (18 How.) at 282); *BMW of N. Am., Inc.* v. *Gore*, 517 U.S. 559, 575 n.22 (1996) (observing that "[t]he strict constitutional safeguards afforded to criminal defendants are not applicable to civil cases") (internal citation omitted).

Far from requiring non-Article III courts to accept the factual determinations of hearing examiners, this Court has rejected claims that due process requires a non-Article III decisional authority to defer to a hearing officer or rehear the evidence firsthand. Thus, in *Morgan* v. *United States*, 298 U.S. 468, 481 (1936) (*Morgan I*), this Court concluded that the Secretary of Agriculture could, consistent with due process, enter factual findings after reviewing only a cold record containing evidence received by a hearing examiner:

> Evidence may be taken by an examiner. Evidence thus taken may be sifted and analyzed by competent subordinates. * * * The requirements are not technical. But there must be a hearing in a substantial sense. And to give the substance of a hearing, which is for the purpose of making determinations upon evidence, the officer who makes the determinations must consider and appraise the evidence which justifies them.

Id. at 481-482.

Similarly, in *NLRB* v. *Mackay Radio & Telephone Co.*, 304 U.S. 333, 350-351 (1938), the Court concluded that due process was not violated by the NLRB's issuance of its own findings and conclusions in a case heard by a trial examiner, even though the Board failed "to follow its usual practice of the submission of a tentative report by the trial examiner and a hearing on exceptions to that report." *Id.* at 350. The court reasoned that so long as "the issues and contentions of the parties were clearly defined and * * * no other detriment or disadvantage is claimed," the parties receive a "full and adequate hearing" within the meaning of the Due Process Clause by the deciding body's review of the cold record. *Id.* at 350-351.

Ballard attempts (Br. 32) to sidestep the clear import of *Morgan I* and *Mackay* by characterizing the proceeding below as "a fraud case." While the imposition of a fraud penalty was at issue here, the proceedings involved solely civil liability under the Internal Revenue Code, and there has been no argument that those penalties are so substantial as to constitute a quasi-criminal penalty. Accordingly, what rule might apply in a criminal case is not at issue here.

In any event, *Raddatz* does not compel the conclusion that the Tax Court's procedures violate due process. In *Raddatz*, this Court considered whether a district court judge could review de novo the credibility assessments of a magistrate judge who had conducted a suppression hearing in a criminal trial. 447 U.S. at 678-681. The Court held that although "courts must always be sensitive to the problems of making credibility determinations on the cold record," *id.* at 679, the Constitution does not preclude de novo review as long as the reviewing court may rehear evidence when making a credibility determination. Such a statutory scheme "includes sufficient procedures to alert the district court whether to exercise its discretion to conduct a hearing and view the

witnesses itself." *Id.* at 680-681. In a subsequent case, the Court confirmed that "[t]he principal constitutional argument advanced and rejected in *Raddatz* was that the omission of a requirement that the trial judge must hear the testimony of the witnesses whenever a question of credibility arises violated the Due Process Clause of the Fifth Amendment. Petitioner has not advanced a similar argument in this case, no doubt because it would plainly be foreclosed by our holding in *Raddatz*." *Peretz* v. *United States*, 501 U.S. 923, 937 (1991).

Tax Court Rule 183 provides precisely the protection deemed sufficient in *Raddatz*, because it authorizes Tax Court judges to "receive further evidence" and "direct the filing of additional briefs" at their discretion. Tax Ct. R. 183(c). Accordingly, the Tax Court's procedures, on their face, satisfy the command of *Raddatz*.

D. Disclosure Is Not Required By *Mathews* v. *Eldridge*

Disclosure of STJ reports is not, contrary to petitioners' claim (03-1034 Br. 17, 25-27; 03-184 Br. 17, 47-48), independently required by *Mathews* v. *Eldridge*, 424 U.S. 319 (1976), which requires a balancing of "the private interest that will be affected by the official action," "the risk of an erroneous deprivation of such interest through the procedures used," "the probable value, if any, of additional or substitute procedural safeguards," and "the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail." *Id.* at 335.

Petitioners were afforded extensive pre-deprivation process: They received notice of the government's claim; a public hearing prior to the government's assessment of tax liability; an opportunity to present evidence during a trial that generated almost 5,500 pages of transcript, more than 4,600 pages of briefs, and thousands of exhibits consuming

hundreds of thousands of pages in the record (03-1034 Pet. App. 3a); a published opinion detailing the Tax Court's reasons for decision, including the factual findings and legal conclusions ultimately recommended by the STJ; and an opportunity to appeal the Tax Court's decision to the federal courts of appeals. In addition, petitioners had the option, which they chose not to exercise, of litigating this dispute in an Article III court by paying the disputed tax and filing a refund action in federal district court.

This process more than satisfies the *Mathews* balancing test. The "private interests" affected by non-disclosure, namely the alleged risk of an "erroneous deprivation" of an individual's funds, are insignificant in light of the extensive hearing petitioners received under the Tax Court's rules. Indeed, this Court held in *Morgan I*, 298 U.S. 468, that a litigant's private financial interest in a civil case does not require an examiner even to prepare a written report, because the litigant's interests are amply protected by the underlying hearing. It follows that such reports need not be disclosed to protect the taxpayers' interests if they are, in fact, prepared. That is particularly true where, as here, the Tax Court judge has adopted the final recommendations of the STJ in full.

In contrast, the government's interest in retaining the current system is substantial. As explained earlier, the broader policy of refusing to disclose non-final reports and other aspects of the deliberative process is vital to the proper functioning of the Tax Court. See pp. 16-17, *supra*. Non-disclosure also eliminates an additional layer of unnecessary and time-consuming review and thus enhances the Tax Court's ability to resolve cases efficiently and to speak with one voice. See pp. 34-36, *supra*. Finally, the government has a substantial interest in tax collection procedures generally, because collection of taxes is "the exercise of a sovereign prerogative, incident to the power to enforce the

obligations of the delinquent taxpayer himself, * * * grounded in the constitutional mandate to 'lay and collect taxes.'" *United States* v. *Rodgers*, 461 U.S. 677, 697 (1983).[11] Because disclosure does not materially advance taxpayer protection, the Tax Court's interest in maintaining its current process must prevail under *Mathews*.[12]

III. DISCLOSURE OF STJ REPORTS IS NOT COMPELLED BY THE INTERNAL REVENUE CODE

Petitioners and their amici suggest in the alternative (03-184 Br. 23; 03-1034 Br. 18, 42-49) that disclosure of STJ reports is compelled by the Internal Revenue Code's appellate review provision, 26 U.S.C. 7482(a)(1), and its disclosure provisions, 26 U.S.C. 7459, 7461. While the Tax Court is required to publish STJ reports to the extent the court adopts the STJ's recommendations, see 26 U.S.C. 7459(b), 7461, petitioners err in contending that an abandoned STJ report must be included in the record.

A. Disclosure Is Not Required Under Section 7482(a)(1)

Internal Revenue Code Section 7482(a)(1) requires that courts of appeals "review the decisions of the Tax Court * * * in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury." 26 U.S.C. 7482(a)(1). Clearly, the "decision[]" that

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[11] For that reason, the Court has tended to take a narrow view of the process required in tax cases. See pp. 30-31, *supra*; *Phillips* v. *Commissioner*, 283 U.S. 583, 595-597 (1931). The more limited reach of due process in the tax context, indeed, suggests that *Mathews* may not provide the proper framework for evaluating the Tax Court's procedures. See *Dusenbery* v. *United States*, 534 U.S. 161, 167-168 (2002) (observing that the Court has "never viewed *Mathews* as announcing an all-embracing test for deciding due process claims").

[12] For the same reason, petitioners' reliance (03-184 Br. 32 n.26) on *Goldberg* v. *Kelley*, 397 U.S. 254 (1970), which also suggests a balancing approach to determine the process due, is misplaced.

Congress intends appellate courts to review under Section 7482(a)(1) is the published opinion of the Tax Court, not the discarded "original" report of an STJ. By its terms, Section 7482(a)(1) identifies the decision for review as the "decision[] *of the Tax Court*" (emphasis added). Throughout the Internal Revenue Code, the term "decision of the Tax Court" is used to mean the decision entered by a regular judge of the Tax Court. Section 7459(a) of the Internal Revenue Code, for example, requires that the "decision[]" of the Tax Court "be made by a *judge* in accordance with the report of the *Tax Court*." 26 U.S.C. 7459(a) (emphasis added).[13] Similarly, Section 7459(b) recognizes that the Tax Court must "include in *its* report upon any proceeding *its* findings of fact or opinion or memorandum opinion." 26 U.S.C. 7459(b) (emphasis added). Where Congress intended entities other than the court's regular judges to enter the "decision[] of the Tax Court," it expressly provided for such entry. In particular, Section 7443A(c) specifies the limited circumstances in which "[t]he court may authorize a special trial judge to make the decision of the court." 26 U.S.C. 7443A(c). Those circumstances do *not* include proceedings like this case, and thus it is clear that an STJ's unadopted "original" report is not the "decision of the Tax Court" subject to appellate review.

It is equally clear that Congress did not intend the "in the same manner" language of Section 7482(a)(1) to import the standards or procedural rules applicable to proceedings before a magistrate judge (see 03-1034 Br. 27-28; Amicus Lederman Br. 11). Rather, the "same manner" requirement was added to clarify the scope of review in Tax Court proceedings after this Court held in *Dobson* v. *Commissioner*, 320 U.S. 489, 501-502 (1943), that Tax Court decisions were

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[13] The Code consistently uses the term "judge" to refer to Tax Court judges, whereas the designation "special trial judge" is used to refer to STJs. *E.g.*, 26 U.S.C. 7456(a) ("any judge *or special trial judge* * * * may administer oaths") (emphasis added).

subject to limited appellate review in light of the then-applicable statutory language requiring appellate courts to determine whether Tax Court decisions were "in accordance with law." *Id.* at 492; see Revenue Act of 1926, ch. 27, § 1003(b), 44 Stat. 9, 110. The "in the same manner" and "to the same extent" language merely clarified that Congress did not intend appellate courts to give special deference to Tax Court decisions.[14] See H. R. Rep. No. 2087, 80th Cong., 2d Sess. 16 (1948) (observing that intention was "to overrule the principle enunciated by the Supreme Court in the Dobson case * * * [which] had the effect of limiting the scope of the review of the cases decided by the Tax Court."); *InverWorld, Ltd.* v. *Commissioner*, 979 F.2d 868, 874 (D.C. Cir. 1992) (observing that Section 7482(a)(1) addresses only scope of review and "was not intended to bind the courts to any particular procedure for determining which *final* decisions are immediately appealable").

B. Disclosure Is Not Required Under Section 7459 Or 7461

Kanter (Br. 42-46) also erroneously reads the Internal Revenue Code's disclosure provisions to require disclosure of original STJ reports. See 26 U.S.C. 7461(a), 7459(b). By their terms, those provisions require disclosure only of reports adopted by the Tax Court.

Section 7461(a) provides that "all reports *of the Tax Court* and all evidence received by the Tax Court and its divisions * * * shall be public records open to the inspection of the public." 26 U.S.C. 7461(a) (emphasis added). Similarly,

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[14] Amicus Professor Leandra Lederman further errs in arguing (Br. 11-22) that STJ reports are evidence that must be included in the record in the same way magistrate judge reports are considered "original evidence" under the Federal Rules of Appellate Procedure. Under federal law, magistrate judges and special masters are *required* to file their reports with the district court and serve them on parties. That is not the case with STJ reports under the Internal Revenue Code. See pp. 33-34, *supra*.

Section 7459(b) provides that "[i]t shall be the duty of the Tax Court and of each division to include in *its* report upon any proceeding *its* findings of fact or opinion or memorandum opinion," and that "[t]he Tax Court shall report in writing all *its* findings of fact, opinions, and memorandum opinions." 26 U.S.C. 7459(b) (emphasis added). The phrase "report of the Tax Court" as used in those provisions is elucidated in Section 7459(a) of the Internal Revenue Code, which creates the "report" requirement. It provides that the report "of the Tax Court" is the document that serves as the basis for the "decision of the Tax Court," and that "[t]he decision *shall* be made by a judge *in accordance with* the report of the Tax Court." 26 U.S.C. 7459(a) (emphases added). Because the STJ's report cannot serve as the Tax Court's decision unless adopted by a judge of the Tax Court, see pp. 24-25, *supra*, reports that are not adopted cannot be the "report of the Tax Court" to which the disclosure requirements refer.

Kanter's attempt to bolster (Br. 43) his reading of those provisions by referencing a single case in which a court "referr[ed] to" the STJ report as the "initial report of the Tax Court," see *Louisville & Nashville R.R.* v. *Commissioner*, 641 F.2d 435, 443 (6th Cir. 1981), is unavailing. A single imprecise choice of words in a lower court opinion that does not consider the meaning of the Internal Revenue Code's disclosure provisions is not persuasive authority as to their meaning. Similarly, Kanter errs in relying (Br. 47-49) on a Senate Report stating that the disclosure provisions "will provide that all such proceedings, records, and evidence in connection therewith shall be public," S. Rep. No. 398, 68th Cong., 1st Sess. Pt. 2, at 12 (1924). The Senate Report does not describe the kinds of documents Congress intended to subject to disclosure, and thus its mere recognition of a disclosure requirement begs the question here.

Kanter's argument, moreover, would lead to absurd results. If abandoned STJ reports were "report[s] of the Tax Court," they would have to be published in the Tax Court's official case reports "for public information and use." 26 U.S.C. 7462. Indeed, Tax Court judges would be barred from modifying STJ reports under Kanter's interpretation of the Code, because Section 7459(a) *requires* the decision of the Tax Court to be "made * * * in accordance with the report of the Tax Court." That result, of course, is plainly contrary to Congress's intent. See 26 U.S.C. 7443A(b)(4) & (c).

Kanter's secondary argument (Br. 40-42) that any report submitted by the STJ is "evidence" within the meaning of the disclosure provisions mistakenly assumes that the STJ functions as a party litigant in the case such that the STJ's statements have "evidentiary" value. The case on which Kanter relies for that argument, *Gonzales* v. *United States*, 348 U.S. 407 (1955), demonstrates the flaw in the argument. In *Gonzales*, this Court held that an individual seeking a deferment from military service was entitled to review a Department of Justice recommendation concerning the deferment request that had been submitted to the Selective Service Appeal Board, the agency with authority to decide the request. *Id.* at 412. The Court reasoned that, because the Department of Justice was the entity framing the arguments against petitioner's deferment request, "petitioner was entitled to know the thrust of the Department's recommendation so he could muster his facts and arguments to meet its contentions." *Id.* at 414. As the Court noted, the "right to a hearing embraces * * * a reasonable opportunity to know the claims of the opposing party." *Id.* at 414 n.5 (quoting *Morgan* v. *United States*, 304 U.S. 1, 18 (1938)). In this case, the opposing party is the Commissioner of Internal Revenue, not the STJ. It is the Commissioner's submissions that frame the arguments against petitioners,

and those submissions are, of course, disclosed and become part of the record. The STJ, in contrast, operates within the adjudicative body itself, and his statements are not evidence.[15]

C. There Is No Common Law Right To Disclosure Of STJ Reports And No Cause For An Exercise Of The Court's Supervisory Powers

Kanter is wrong to claim (Br. 44-46) that the "common-law" right of access extends to STJ reports. Indeed, because the question whether disclosure is compelled by an alleged "common law right" is not fairly contained in the questions presented, it is not a question that this Court should review. See Sup. Ct. R. 14.1(a). In any event, the common law right has never been interpreted to extend to a court's internal deliberations. Thus, the public has no right of access to court conferences, draft opinions, or internal court memoranda, just as a party has no right to take discovery of a judge's thought processes. See pp. 16-17, *supra*.

Nor would an exercise of this Court's supervisory powers be appropriate. Again, that issue is not fairly included in the questions presented. In any event, the exercise of supervisory power sought by Kanter (03-1034 Br. 49-50) would be outside the normal scope of that power. This Court has never exercised its supervisory authority to alter the rules of an Article I tribunal, such as the Tax Court, that has been vested by Congress with exclusive authority to promulgate its own rules, and it should not do so here. See 26 U.S.C. 7453, 7443A; compare 26 U.S.C. 2071(a) & 2072(a) (conferring authority on this Court to prescribe rules for itself and for district courts, magistrates, and courts of appeals, but not the Tax Court); see also *Dickerson* v. *United States*, 530 U.S.

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[15] Kanter also characterizes this argument (Br. 39-42) as implicating his right to an effective "hearing" before the Tax Court. That issue is not fairly included within the questions presented, which are limited to issues of appellate review.

428, 437 (2000) ("supervisory authority over the federal courts" is subject to "ultimate authority" of Congress absent constitutional constraints).

CONCLUSION

The judgments of the courts of appeals should be affirmed.

Respectfully submitted.

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OCTOBER 2004

APPENDIX

1. 26 U.S.C. 7443A (1994) provided in pertinent part:

Special trial judges

(a) Appointment. The chief judge may, from time to time, appoint special trial judges who shall proceed under such rules and regulations as may be promulgated by the Tax Court.

(b) Proceedings which may be assigned to special trial judges. The chief judge may assign—

(1) any declaratory judgment proceeding,

(2) any proceeding under section 7463,

(3) any proceeding where neither the amount of the deficiency placed in dispute (within the meaning of section 7463) nor the amount of any claimed overpayment exceeds $10,000, and

(4) any other proceeding which the chief judge may designate,

to be heard by the special trial judges of the court.

(c) Authority to make court decision. The court may authorize a special trial judge to make the decision of the court with respect to any proceeding described in paragraph (1), (2), or (3) of subsection (b), subject to such conditions and review as the court may provide.

* * * * *

2. 26 U.S.C. 7459(a) and (b) provide:

Reports and decisions

(a) Requirement. A report upon any proceeding instituted before the Tax Court and a decision thereon shall be made as quickly as practicable. The decision shall be made by a judge in accordance with the report of the Tax Court, and such decision so made shall, when entered, be the decision of the Tax Court.

(b) Inclusion of findings of fact or opinions in report. It shall be the duty of the Tax Court and of each division to include in its report upon any proceeding its findings of fact or opinion or memorandum opinion. The Tax Court shall report in writing all its findings of fact, opinions, and memorandum opinions. Subject to such conditions as the Tax Court may by rule provide, the requirements of this subsection and of section 7460 are met if findings of fact or opinion are stated orally and recorded in the transcript of the proceedings.

* * * * *

3. 26 U.S.C. 7460(b) provides:

Provisions of special application to divisions

(b) Effect of action by a division

The report of the division shall become the report of the Tax Court within 30 days after such report by the division, unless within such period the chief judge has directed that such report shall be reviewed by the Tax Court. Any preliminary action by a division which does not form the basis for the entry of the final decision shall not be subject to review by the Tax Court except in accordance with such rules as the Tax

Court may prescribe. The report of a division shall not be a part of the record in any case in which the chief judge directs that such report shall be reviewed by the Tax Court.

4. 26 U.S.C. 7461(a) provides:

Publicity of proceedings

(a) General rule. Except as provided in subsection (b), all reports of the Tax Court and all evidence received by the Tax Court and its divisions, including a transcript of the stenographic report of the hearings, shall be public records open to the inspection of the public.

5. 26 U.S.C. 7462 provides:

Publication of reports

The Tax Court shall provide for the publication of its reports at the Government Printing Office in such form and manner as may be best adapted for public information and use, and such authorized publication shall be competent evidence of the reports of the Tax Court therein contained in all courts of the United States and of the several States without any further proof or authentication thereof. Such reports shall be subject to sale in the same manner and upon the same terms as other public documents.

6. 26 U.S.C. 7482(a)(1) provides:

Courts of review

(a) Jurisdiction.

(1) In general. The United States Courts of Appeals (other than the United States Court of Appeals

for the Federal Circuit) shall have exclusive jurisdiction to review the decisions of the Tax Court, except as provided in section 1254 of Title 28 of the United States Code, in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury; and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 1254 of Title 28 of the United States Code.

7. Tax Court Rule 183 provides:

Other Cases

Except in cases subject to the provisions of Rule 182 or as otherwise provided, the following procedure shall be observed in cases tried before a Special Trial Judge:

(a) Trial and Briefs: A Special Trial Judge shall conduct the trial of any such case assigned for such purpose. After such trial, the parties shall submit their briefs in accordance with the provisions of Rule 151. Unless otherwise directed, no further briefs shall be filed.

(b) Special Trial Judge's Report: After all the briefs have been filed by all the parties or the time for doing so has expired, the Special Trial Judge shall submit a report, including findings of fact and opinion, to the Chief Judge, and the Chief Judge will assign the case to a Judge or Division of the Court.

(c) Action on the Report: The Judge to whom or the Division to which the case is assigned may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive

further evidence or may direct oral argument, or may recommit the report with instructions. Due regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct.

8. Tax Court Rule 182 (1974) provided:

Post-Trial Procedure

Except in small tax cases (see Rule 183) or as otherwise provided, the following procedure shall be observed in cases tried before a commissioner:

(a) Proposed Findings and Briefs: Each party shall file his initial brief, including his proposed findings of fact and legal argument, within 60 days after the date on which the trial is concluded, unless otherwise directed. A party thereafter desiring to file a responsive brief shall do so, including any objections to any proposed findings of fact, within 30 days after the expiration of the period for filing the initial brief, unless otherwise directed. With respect to the content, form, number of copies, and other applicable requirements, the proposed findings of fact and the briefs shall conform to the provisions of Rule 151.

(b) Commissioner's Report: After all the briefs have been filed by all the parties or the time for doing so has expired, the commissioner shall file his report, including his findings of fact and opinion. A copy of the report shall forthwith be served on each party.

(c) Exceptions: Within 45 days after service of the commissioner's report, a party may file with the Court a brief setting forth any exceptions of law or of fact to that report. Within 30 days of service upon him of such brief, any other party may file a brief in response thereto. In any brief filed pursuant to this paragraph, a party may rely in whole or in part upon the briefs previously submitted by him to the commissioner under paragraph (a) of this Rule 182. Unless a party shall have proposed a particular finding of fact, or unless he shall have objected to another party's proposed finding of fact, the Court may refuse to consider his exception to the commissioner's report for failure to make such a finding desired by him or for inclusion of such finding proposed by the other party, as the case may be.

(d) Oral Argument and Decision: The Division to which the case is assigned may, upon motion of any party or on its own motion, direct oral argument. The Division inter alia may adopt the commissioner's report or may modify it or may reject it in whole or in part, or may receive further evidence, or may recommit it with instructions. Due regard shall be given to the circumstance that the commissioner had the opportunity to evaluate the credibility of witnesses; and the findings of fact recommended by the commissioner shall be presumed to be correct.

9. Tax Court Rule 48 (1944) provided:

Commissioners of the Tax Court

(a) The term "commissioner" as used in this Rule 48 applies to any attorney on the legal staff of this Court who shall have been designated by the

Presiding Judge as a "commissioner in a particular case" pursuant to section 1114 of the Internal Revenue Code, as amended by section 503 of the Revenue Act of 1943.

(b) The commissioner shall conduct the hearing in such case in accordance with the Court's rules of practice. He shall rule upon objections and other evidentiary matters in accordance with the rules of evidence as provided in section 1111, and shall exercise such further and incidental authority, including the issuance of subpoenas, as may be necessary for the conduct of the hearing.

(c) Unless otherwise directed the parties shall have 30 days from the closing of proof in the case for filing proposed findings of fact. Such findings of fact shall be prepared in the manner and form prescribed in the first paragraph of Rule 35(b).

Upon the filing by the parties of their proposed findings of fact, the commissioner shall prepare and submit to the Court or a Division thereof a report of his findings of fact based upon the evidence in the case, and copies thereof shall be served upon both parties.

Within 20 days from the filing of the commissioner's proposed findings of fact the parties may file exceptions thereto which will be considered by the Division to which the case is assigned.

(d) Unless otherwise directed by the Court, the parties shall have 45 days from the date of the filing of the commissioner's proposed findings of fact within which to file briefs, and 15 days additional

within which to file reply briefs. Each brief shall be prepared in the manner and form prescribed in Rule 35.

(e) Upon motion of either party, or upon its own motion, the Division to which the case is assigned may in its discretion direct oral argument and set a date therefor.

10. United States Tax Court General Order Number 5 (1976) provided:

Additional Cases Assigned to Special Trial Judges

A. Purpose

Both the number of new cases filed in the United States Tax Court and the total number of cases involving deficiencies under $2,500 have increased substantially in the past year, and there is reason to believe that the work of the Court will continue at a higher level. Thus, it appears advisable to make changes in the present practices of the Court in order to dispose of pending cases more promptly and efficiently. To accomplish those objectives, it has been decided that additional cases should be assigned to the Special Trial Judges of the Court for trial or other disposition.

B. Cases Assigned

The Court has followed the practice of assigning most of the "small tax cases" to Special Trial Judges for trial or other disposition. The work of the Court has been reviewed for the purpose of deciding what additional cases could be assigned to the Special Trial Judges. We have sought to select

cases in which the parties would find a trial by the Special Trial Judges to be most suitable. In the light of this criterion, it appears appropriate to assign to the Special Trial Judges additional cases involving relatively small deficiencies.

C. Procedures

1. In accordance with this order and Rule 180, Tax Court Rules of Practice and Procedure, the Chief Judge may assign to a Special Trial Judge for trial or other disposition cases which are not "small tax cases" as defined in Rule 171, Tax Court Rules of Practice and Procedure, but in which the amount of the deficiency in income or gift taxes does not exceed $2,500 in any one taxable year or the deficiency in estate tax does not exceed $2,500.

2. All proceedings in cases assigned to Special Trial Judges in accordance with this order shall be conducted in accordance with the Tax Court Rules of Practice and Procedure, and the Special Trial Judges shall have all the powers described in Rule 181. However, Rule 182 provides in part that its provisions are applicable "[e]xcept in small tax cases (see Rule 183) or as otherwise provided." Since the amount at issue is small in the cases assigned to the Special Trial Judges in accordance with this order, it is clearly impracticable and undesirable to follow the post-trial procedures set forth in Rule 182. Accordingly, pursuant to the authority of such rule to provide otherwise, it has been decided that such procedures shall not be applicable in the cases assigned to the Special Trial Judges in accordance with this order.

3. If either party objects to having the case tried in accordance with the procedures established by this order, he may file a motion to that effect within 15 days after service of the notice setting the case for trial before a Special Trial Judge, setting forth his objections to having the case so conducted. In considering such motion, the Court will take into consideration the amount in controversy, the significance of the matter at issue, the convenience of the parties, and the responsibilities of the Court.

D. Opinions

As soon as practicable after hearing a case assigned to him in accordance with this order, a Special Trial Judge shall prepare his proposed findings of fact and opinion and submit them to the Chief Judge, or to another Judge designated by him for that purpose. The proposed findings of fact and opinion of the Special Trial Judge shall not constitute the findings of fact and opinion of the Court unless reviewed and adopted by the Judge to whom the case is assigned, and the report is approved by the Chief Judge.

(11)

No. 03-1034

In the Supreme Court of the United States

ESTATE OF BURTON W. KANTER, ET AL.,
PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

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INTRODUCTION

The IRS's legal arguments all rest on a single, but obviously flawed premise: that the Rule 183 report of the trial judge cannot be disclosed because it is part of the internal "deliberative process" of the Tax Court. But this report communicates the recommended findings of fact from the trial judge following a formal trial in which constitutionally protected property and liberty interests are at stake. The Rule 183 report is the sole record of the unfiltered, independent findings of the only judge who has heard the witnesses; the report must be officially submitted to the Tax Court; and this report forms the foundation for all subsequent Tax Court review of the report's recommended findings. The Tax Court's own rules — consistent with the unique role of a trial judge in a formal adjudication — require that court to give special deference to the Rule 183 findings. Indeed, as Judge Cudahy concluded, there is "no single item of more significance in evaluating a Tax Court's decision on fraud than the unfiltered findings of the STJ." Pet. App. 93a. There is no conceivable basis on which such a report, which has such direct and substantial legal consequences, can be suppressed as a matter of internal "deliberative process."

The IRS obscures this central reality by attacking straw man arguments that petitioners have never raised — such as the argument that Tax Court personnel must be deposed or that their honesty may be impeached. Petitioners, of course, have never asked for anything of the sort. Petitioners simply argue that the Rule 183 report must be disclosed to the litigants and be part of the record to ensure legally proper appellate review. The Tax Court cannot frustrate the right to proper Article III judicial review that Congress has conferred in 26 U.S.C. 7482(a)(1). To a busy appellate court, dramatic conflicts between the independent and unfiltered findings of the trial judge and those of the reviewing Tax Court judge would immediately become the central focal point for appellate review. The Tax Court has made sure the appellate courts are never even aware of any such conflicts.

The IRS disputes none of the critical facts. Over $30,000,000 in tax liabilities are at issue here, most of which consists of quasi-criminal penalties for alleged fraud. Nor has the IRS denied the ruinous reputational consequences the finding of fraud had for a businessman such as Ballard or a tax attorney such as Kanter and the special need for procedural fairness that these consequences create. The IRS does not deny that it must establish fraud by clear and convincing evidence. Nor does it deny that an experienced trial judge originally found that there was no fraud. The IRS does not deny that the Tax Court completely rewrote the report of STJ Couvillion, overturning all his original, independent findings of credibility and reversing his conclusion that there was no underpayment of taxes and no evidence of fraud. Kanter Br. App. 6a. Nor has the Commissioner denied that the Tax Court concealed this situation from the reviewing courts by reciting that the STJ and Tax Court judge were in agreement, without revealing this remarkable *volte-face* or offering the slightest explanation for it. As the Dick affidavit testifies, three judges of the Tax Court came forward to report these facts, including Chief Special Trial Judge Panuthos, perhaps speaking on behalf of all the STJs, who serve at-will. Kanter Br. App. 6a. Even in this Court the IRS plays a game of cat and mouse by referring to the original STJ report as "abandoned" without "conceding" that the Rule 183 report contained findings and conclusions that overwhelmingly supported the taxpayers. Br. 15-16, 22-23.

The D.C. Circuit's decision in *Stone* illustrates the value the STJ report has for appellate courts discharging their Article III responsibilities. Based on credibility determinations in the STJ's original report, *Stone* found "clear error" in the Tax Court's decision to reject those determinations. *Stone* v. *Comm'r*, 865 F.2d at 347-352. It is no surprise that the Tax Court changed its rule in the midst of that litigation hoping to insulate from subsequent appellate review those decisions in which it reversed, as here, the STJ findings. Already in this case, another participant in the very same transactions has

been cleared of any charge of tax fraud in his recent appeal to the Fifth Circuit. *Lisle* v. *Comm'r*, 341 F.3d at 375-383. That the trial judge independently reached the same conclusion about all three taxpayers would surely be relevant to proper appellate review. Even if the Tax Court judge and the trial judge later "collaborated" on creating new credibility findings — if due process permits such a thing — the original, independent, and unfiltered findings of the trial judge would remain just as essential to proper appellate review.

As amicus business and public-interest groups seeking to ensure fair trials in the Tax Court agree, Judge Cudahy was correct in concluding that due process requires disclosure of the STJ's report. He was also correct in concluding that Congress's command in 26 U.S.C. 7461(a) that "all reports" of Tax Court judges (including STJs) be disclosed applies here and reinforces the requirements of due process.

1. The Commissioner's newly invented "two-report" rationalization flies in the face of the Tax Court's rule and contradicts its own prior decisions in this case.

In an effort to salvage the bizarre practice of preparing trial judge findings that are legally presumed correct, yet nonetheless kept secret, the Commissioner offers this Court (Br. 14-15, 22-23) a description of Tax Court procedure that cannot be squared with the plain language of the Tax Court's rules or with the Tax Court's own prior decisions in this case. The Commissioner now argues that the practice of the Tax Court is for the STJ to file *two* reports. In making this argument, the Commissioner is forced to fabricate an entirely new set of terms — none of them found in the relevant statutes or Tax Court rules. The Commissioner acknowledges that STJ Couvillion did officially file his Rule 183 report and he does not deny that the report found no fraudulent intent. But the Commissioner refuses to admit that this report is "*the* Special Trial Judge report" referred to in Rule 183(c) (emphasis added). Instead, the Commissioner argues that the report STJ Couvillion filed under Rule 183 is merely an "original re-

port." According to the Commissioner, STJ Couvillion filed a *second* report. The Commissioner sometimes calls this second report the "final report" of the STJ; other times, he calls it the "ultimate recommended findings" of the STJ; yet other times, he calls it the STJ's "final recommended disposition." Br. 14-23. In other words, the required Rule 183 report that STJ Couvillion filed is merely an "original report" which the STJ "subsequently abandoned."

This contrived terminology is designed to support the claim that the Rule 183 report is protected deliberative material. But not only does this "two-report" rationalization fail to do so, it reveals how unlawful the Tax Court's practice is. First, Rule 183 does not authorize or in any way contemplate the filing of two distinct STJ reports. By its plain language, Rule 183(b) requires that "the Special Trial Judge shall submit *a* report, including findings of fact and opinion" (emphasis added). Rule 183(c) authorizes the Tax Court judge to "adopt *the* Special Trial Judge's report" or to "modify it" or to "reject it in whole or in part" (emphasis added). The definite article "the" obviously requires the Tax Court judge to review *the* Report that must be filed under Rule 183. *Freytag* v. *Commissioner*, 501 U.S. at 902 (Scalia, J., concurring) ("The definite article 'the' obviously narrows the class"). The Rule refers to one report and one set of findings. The invented terms "original" and "final" reports or "ultimate recommended findings" appear nowhere in the Rule or statutes. The Tax Court might prefer a system of adjudication in which the trial judge issues two reports, one kept secret and the other jointly authored with the reviewing judge. But that is not the system created by law.

Second, Rule 183(c) requires that "the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." This plainly refers to "the findings of fact" set forth in the Rule 183 report. Rule 183(c) also requires the Tax Court to give "due regard" to the fact "that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses." These provisions reflect the fundamental divi-

sion of labor that characterizes American judicial practice: the trial judge makes findings of fact, and the reviewing judge — under the relevant standard — reviews those findings. But the Commissioner's theory makes this provision in the Tax Court's rules utterly incoherent. According to the Commissioner, the Tax Court is required to presume correct only the findings in the "final" report of the STJ, yet the findings in that "final STJ report" are ones the Tax Court judge and the STJ have jointly created. Obviously, the Tax Court judge cannot "presume correct" or defer to findings of fact which he himself has crafted. How can the Tax Court judge review his own findings? The Rule requires that the Tax Court judge presume correct and give "due regard" to findings *in some other document* the Tax Court judge himself has not created: that document is the Rule 183 report that the STJ is required to file and which reflects the STJ's independent recommended findings.

Third, the Commissioner's brief before this Court contains the first suggestion by anyone, anywhere that STJ Couvillion filed two reports. In his Order denying petitioners' motion for access to the STJ's report, Judge Dawson wrote:

> After a lengthy trial, * * * Special Trial Judge Couvillion submitted his report containing findings of fact and opinion pursuant to Rule 183(b), which ultimately became the Memorandum Findings of Fact and Opinion (T.C. Memo. 1999-407) filed on December 15, 1999. In accordance with Rule 183(c), the Chief Judge referred the cases to Judge Dawson for review and, if approved, for adoption. In reviewing the Special Trial Judge's report, Judge Dawson gave due regard to the fact that Special Trial Judge Couvillion evaluated the credibility of witnesses * * *. Pet. App. 108a.

Judge Dawson's order refers to only *one* STJ report, the one required to be filed and reviewed under Rule 183. Likewise, an Order issued by the Chief Judge informed the parties that Judge Couvillion had filed "a report, as required by Rule 183(b)" and that the case was then assigned to Judge Daw-

son. Pet. App. 113a-114a. The Chief Judge's Order refers to only one report of the STJ and makes clear that it is that report — not some "second" or "final" report — that Judge Dawson was to review. *Ibid.* The Commissioner's assertion that the STJ filed two reports, and that in seeking the STJ's Rule 183 report petitioners seek to invade the STJ's "deliberative process," is flatly inconsistent with the Tax Court's own orders. And if the STJ did in fact file two reports, then the Courts of Appeals were seriously deceived by the official orders of the Tax Court.

The Commissioner is forced into more and more indefensible positions as he struggles to bring his new "two-report" theory into line with the actual language of Rule 183. The Commissioner urges this Court "to invalidate the offending language in the rule" — that is, the "due regard" and "presumed to be correct" language in Rule 183. Br. 29 n.7. According to the Commissioner, if Rule 183 gives litigants the right to ensure that the recommended findings of the trial judge are properly given due regard and presumed correct, then this Court should simply "invalidate" the Rule's "offending language." But this remarkable argument cites no authority that would permit the Court simply to "invalidate" legally binding language in a validly promulgated rule. "So long as this regulation is extant it has the force of law." *United States* v. *Nixon*, 418 U.S. 683, 695 (1974). The Tax Court, like other entities in the judicial or executive branches, has discretion to decide whether to adopt certain rules. But once it adopts a rule, the Tax Court is legally obligated to comply with it. See *United States ex rel. Accardi* v. *Shaughnessy*, 347 U.S. 260, 265-267 (1954); accord *Service* v. *Dulles*, 354 U.S. 363, 388 (1957); *Vitarelli* v. *Seaton*, 359 U.S. 535, 539-545 (1959).

Finally, the Commissioner intimates that Rule 183 should be construed as merely an internal procedural directive to "guide" Tax Court judges, rather than as an enforceable command that trial judge findings "shall be presumed to be correct." Br. 26-29. But Rule 183 governs the *substantive*

legal weight to be given to recommended findings of fact of the trial judge. The Rule uses the mandatory term "shall" twice. The Commissioner points to no instance in which rules governing the legal weight to be given to judicial findings are treated as mere internal guidelines. The D.C. Circuit in *Stone* reversed the Tax Court precisely because the Tax Court had not properly applied the presumption of correctness to an STJ's findings. As *Stone* recognized, Rule 183 creates legal rights rather than just providing internal guidance.

The Commissioner's "two-report" rationalization is, therefore, virtually a confession that the Tax Court has violated its own rules and has no basis for concealing the original report. Rule 183 requires the STJ to file a report and requires the Tax Court judge to give deference to the findings in *that* report. Rule 183 does not permit the Tax Court judge to ignore the findings in the Rule 183 report but "defer" to findings in a second report for which the Tax Court judge himself served as contributing author and editor-in-chief. The Commissioner has described an idiosyncratic system of adjudication (of doubtful constitutional validity) that the Tax Court might adopt. But one thing is certain: that system is not the one Rule 183 currently creates.

There is only one Rule 183 report. The critical statement by the only judge who heard the witnesses is that contained in the Rule 183 report submitted to the Chief Judge because that is where the STJ is required by law to state his findings and opinion and it is the findings in that document that have legally operative weight. The Rule 183 report, therefore, cannot possibly be an internal document protected by deliberative privilege. It is not a law clerk's bench memo, nor a draft, but an officially submitted report with a legally operative set of findings. This report was required to be disclosed and served on the parties for over 40 years prior to the 1984 amendment of Rule 183, which belies the claim that keeping the report secret is "vital to the proper functioning of the Tax Court." IRS Br. 40.

The Commissioner's entire argument hinges on the false premise that the Rule 183 report is protected as part of the internal "deliberative process" of the Tax Court. Once that argument is rejected, the Commissioner has almost nothing left to say to refute petitioners' demonstration that due process and federal statutes require the Rule 183 report to be part of the record to enable proper appellate review.

2. Suppression of the STJ report violates Due Process and the appellate review statute.

Due process requires that the original, independent and presumptively-correct findings of the trial judge be part of the record on review. Suppression of the Rule 183 report also frustrates the appellate review statute, 26 U.S.C. 7482, which requires that appellate review of Tax Court decisions be just as thorough as review of District Court decisions, where magistrate findings of fact are treated as essential to appellate review. See Lederman Amicus Br. 9-22.

Petitioners and many supporting amici have shown that in every federal judicial and administrative context other than the Tax Court, Congress and the federal judiciary have concluded that fair, accurate adjudication requires inclusion in the record of the recommended findings of the original trier of fact. That is true whether the original factfinder is a hearing officer, magistrate judge, administrative law judge, special master, or bankruptcy judge. The same principle must surely apply to a formal adjudication before a judicial tribunal of the United States in which constitutionally protected property and liberty interests are at stake and in which the trial judge is the only judicial officer who has heard the testimony of the witnesses. Similarly, disclosure is always required even when (as in the agency context) the original, recommended findings are not presumed correct and the ultimate decisionmaker exercises de novo review over the facts. Disclosure must surely be at least as central to fair, accurate adjudication when — as even the Commissioner and Tax Court concede here — the Tax Court is *required by law*

to give deference to the STJ findings under the "due regard" and "presumed correct" standards of Rule 183.

There are at least three reasons why federal judicial and administrative practice everywhere require disclosure of original findings. The Commissioner's brief ignores all these reasons. First, as Judge Cudahy concluded, an appellate court cannot properly undertake the statutorily required clearly-erroneous review of Tax Court decisions without the original findings of the STJ who presided at trial. To undertake clearly-erroneous review, *Anderson* v. *City of Bessemer City* requires that appellate courts give "even greater deference to the trial court's findings" (470 U.S. at 575) on credibility matters than to other findings to which clearly-erroneous review also applies. Judge Cudahy rightly concluded that if appellate courts must give exceptionally great deference on credibility to triers of fact, "we must inevitably give less deference to the judge who subsequently reverses those findings." Pet. App. 90a. But faced with Tax Court decisions that completely obscure authorship of the findings of fact, even on credibility, the courts of appeals have no idea whose findings they are reviewing. The Tax Court's decision *appears* to "adopt" the findings of the STJ. The Commissioner's brief now argues, however, that these findings are actually the product of joint "collaboration" by the Tax Court judge and the STJ. If the findings were authored by the Tax Court judge, in whole or in part, the court of appeals would commit legal error in giving them the "greater deference" *Anderson* requires for findings independently made by the trial judge. Yet, if the findings are exclusively those of the STJ who actually heard the witnesses, the court of appeals would commit legal error in *not* giving those credibility findings the "greater deference" *Anderson* requires. The Tax Court's practice makes it impossible for the court of appeals to know *who* has authored these findings and therefore how to apply the proper legal standard of review.

Second, as Justice Frankfurter famously observed in *Universal Camera*, reasoned decision making and common sense

require recognition "that evidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion." 340 U.S. at 496. Accordingly, "[t]he substantiality of evidence must take into account whatever in the record fairly detracts from its weight." *Id.* at 488. Conflicts between the STJ — who plays a far more substantial judicial role than a hearing examiner — and the Tax Court judge must be on the record for the court of appeals properly to determine whether the evidence supporting the Tax Court's conclusions meets the clearly erroneous standard. When the Tax Court expunges these conflicts from the record (even if the Tax Court judge secretly collaborates with the STJ on a new opinion in which the Tax Court "persuades" the STJ to change his mind), the appellate courts are precluded from an essential aspect of proper review. This is all the more apparent in Tax Court cases, in which factual issues are exceptionally complex and appellate courts are likely to affirm factual findings absent any indication of conflict below. In view of these concerns, federal appellate courts consistently have held that decisionmakers must overtly address findings of hearing officers and state sufficient reasons for overturning them (Kanter Br. 35-36 n.15) — not conceal the discrepancy.

Third, failure to disclose the STJ report prevents the appellate court from determining whether the Tax Court has properly followed the law. The Tax Court and petitioners agree that Rule 183 requires the Tax Court to give at least some deference to the STJ's findings in his Rule 183 report. The parties differ over precisely what level of deference is required, but that deference is legally owed is not disputed. Yet, it is literally impossible for the courts of appeals to determine whether the Tax Court has given the required deference to the Rule 183 findings if the record does not include those findings. Congress granted the right to full appellate review to ensure that, among other things, the Tax Court

complied with the law. Secret STJ reports obviously frustrate this congressional design. Congress's constitutional power to allocate the initial adjudication of "public rights cases," such as tax disputes, to non-Article III courts depends on the presence of later Article III court review of all questions of law decided in Article I tribunals. Ballard Br. 24-25; Kanter Br. 38 n.18. But the Article III courts cannot determine whether the Tax Court has complied with Rule 183 absent the STJ's Rule 183 report.

Moreover, the original credibility findings in a formal adjudication of a trial judge or other factfinder have a special constitutional status. As this Court suggested in *Raddatz*, 447 U.S. at 681 n.7 — and as lower courts have uniformly concluded — a district court would violate due process were it to reject a magistrate's proposed credibility findings in a suppression hearing without the district court itself hearing the key witnesses. A tax fraud proceeding in which the government seeks millions of dollars in penalties would inflict serious reputational injuries that implicate constitutionally protected property and liberty interests. See *McKesson*, 496 U.S. at 36-37; *Comm'r* v. *Shapiro*, 424 U.S. 614, 629-633 (1976); *Oberg*, 512 U.S. at 430-432. At a minimum, *Raddatz* and due process must require that the independent credibility findings of the trier of fact be included in the record so that any reversal of those findings by the Tax Court (or the Tax Court in collaboration with the STJ) can be adequately assessed by the appellate courts.

"As this Court has stated from its first due process cases, traditional practice provides a touchstone for constitutional analysis." *Oberg*, 512 U.S. at 430. Petitioners and amici have demonstrated that in every area of federal judicial and administrative practice, the long-established rule is that the initial, recommended findings of a hearing officer are a critical element of the decisional process that must be disclosed and made part of the record. Disclosure of a report that is already required to be prepared and officially filed would impose no burden on the government. Petitioners contend

that due process *always* requires that trial judge findings that carry *legally operative weight* be made part of the record. Under the balancing test of *Eldridge* as well, due process requires such disclosure.

None of this analysis changes even if the Tax Court rules and congressional statutes permit — as they do not — the Tax Court to change its procedures in the middle of a trial. Even if the Tax Court judge is somehow permitted under Rule 183 to collaborate and "influence" the STJ (IRS Br. 20) to jointly author a new, second opinion that completely repudiates the STJ's independent and original findings, due process would still require that the Rule 183 report be part of the record. Regardless of what else happens, the Rule 183 report includes findings that must be treated as presumptively correct and given due regard, and this report contains the only record of the original, independent findings of the one judge who has heard the witnesses.

The Commissioner ignores the distinct role of the trial judge or original finder of fact in an Article I or Article III court. The Tax Court judge and the trial judge are not akin to appellate judges "jointly hearing a case as a panel." IRS Br. 21. They are, as even the Commissioner concedes, a trial judge who tries the case and submits a required report with recommended findings of fact, and a Tax Court judge who must review that report and decide whether — under the relevant standard of review — to modify, adopt, or reject proposed findings. Whatever the scope of the Tax Court's power to modify recommended findings, it remains the case that the Tax Court judge has not heard a single witness. Any procedure in which the credibility judgments of a trial judge who has heard the witnesses could be "influence[d]" (IRS Br. 20) before being finalized by a judge who is to review those judgments but has not heard the witnesses would raise troubling constitutional issues under *Raddatz* and the basic due process right to be heard. Those issues are adequately addressed at this stage by requiring that the original, independ-

ent and presumptively-correct findings of the trial judge be part of the record the appellate courts review.

That the STJ who is hired and serves at the pleasure of the Tax Court has no structural protection in office — not even that of an ALJ or magistrate — must also be kept in mind. As Judge Cudahy noted, "the STJs are not equal to the Tax Court judges." Pet. App. 95a. See also Winwood, *The Reclusive Report: The Tax Court Denies Due Process by not Disclosing Special Trial Judge Reports*, 2004 Fed. Cts. L. Rev. 3, ¶ III.A.1 (noting that STJs "may be removed from service without restriction"). To take account of this structural dependence is not to cast doubt on the honesty or integrity of STJs or Tax Court judges. It is simply to acknowledge the reality that underlies Article III of the Constitution and that also has characterized this Court's separation-of-powers caselaw: the power of a superior to remove an officeholder includes the power to influence, in subtle as well as overt ways, the subordinate's decisionmaking. See, *e.g.*, *Bowsher* v. *Synar*, 478 U.S. 714, 725-731 (1986); *Morrison* v. *Olson*, 487 U.S. 654, 682-697 (1988). In the nearly 900 decisions since STJ reports became secret, there is not a single instance in which the Tax Court judge and the STJ have disagreed on the record. Pet. App. 74a.

As Justice Scalia noted in his *Morrison* dissent, the purpose of structural guarantees is, ultimately, "to preserve individual freedom." 487 U.S. at 727 (Scalia, J., dissenting). A taxpayer charged with tax fraud must have the right to see the presumptively correct findings of the only judge who tried the case — whether or not that trial judge has authority to "collaborate" with a superior in producing a dramatically altered, second set of findings. *Morgan*, 304 U.S. at 16-22. The taxpayer also has the right to know whether findings, such as those on credibility, have been altered, and if so, for what reason.

Against all this, the Commissioner points to only two situations in which the findings of a trial judge or initial hearing officer are not disclosed. But neither context is analo-

gous. In the rare instance in which the full Tax Court decides to engage in en banc review of the proposed opinion of a single Tax Court judge, that proposed opinion is, by statute, excluded from the record. See 26 U.S.C. 7460(b). Of course, Section 7460(b) shows that, when Congress prefers special rules for the use of certain Tax Court reports, it knows how to provide them. But in any event, this statutory provision is irrelevant here.

As the Tax Court itself has made clear, Section 7460(b) proceedings are reserved for broad legal issues that warrant full Tax Court consideration in exceptional circumstances. The en banc process is not designed to review findings of fact made by the judge who has presided at trial. Cases warranting full court review "are generally ones that (1) decide legal issues not previously considered by the Tax Court; (2) invalidate a Treasury regulation; (3) would conflict with existing Tax Court case law; (4) involve a legal issue not previously considered by the Tax Court, and, as written, would conflict with the decision of a Court of Appeals other than the one to which appeal would lie; or (5) involve an issue on which the Tax Court was previously reversed by a circuit other than the one to which appeal would lie." Leandra Lederman & Stephen W. Mazza, TAX CONTROVERSIES: PRACTICE AND PROCEDURE 247 (2000). The Chief Judge of the Tax Court has confirmed that Section 7460 review is limited to those circumstances. See App. A to the ABA REPORT OF TASK FORCE ON CIVIL TAX LITIGATION PROCESS (1989).

Just as importantly, Rule 183(c) *requires* the Tax Court to defer to the findings of the Special Trial Judge under the "presumed correct" and "due regard" standards. There is no similar legal requirement when the full Tax Court reviews a single Tax Court judge's opinion. Moreover, the original Tax Court judge (who, unlike an STJ, is legally a peer of the other Tax Court judges) sits with the full Tax Court in this en banc process and, unlike the Special Trial Judge, can issue a dissent. Congress did not design the Section 7460(b) en banc review process as a means through which the Tax Court

could reverse the trial judge's findings of fact. But should the Tax Court attempt to do so, the original Tax Court judge — unlike the STJ — can publish his or her original findings. See Kafka & Ackerman, *Fact-Finding in the Tax Court: Access to Special Trial Judge Reports*, 91 Tax Notes 639 (2001).

After searching far and wide for any other situation in which original trial judge findings are not disclosed, the IRS can only point to the process by which government contract disputes are resolved. Br. 31-32. Of course, the interests at stake in executive-branch contract-dispute resolution are hardly comparable to those involved in judicial proceedings before the Tax Court in which the government seeks millions of dollars in fraud penalties against individual citizens. Nor have contract disputes given rise to the sort of controversy between the government and citizens that has led Congress to demand exceptional transparency and accountability in the adjudication of tax disputes.

Even so, the bodies that decide such disputes have structural safeguards that preclude the kind of unfairness that occurred here. The presiding judge whose original decision is reviewed by a board of contract appeals is a peer not dependent for continued employment on the other judges; he is a full participant in issuance of the final decision and can file a dissent. In addition, boards of contract appeals have made clear that they stand ready to provide *any* material needed by the reviewing court of appeals. For example, Rule 137 of the board of contract appeals for the General Services Administration, codified at 48 C.F.R. 6101.37(a), states that "[w]hen a party has appealed a Board decision to the United States Court of Appeals for the Federal Circuit, the record on review shall consist of the decision sought to be reviewed, the record before the Board * * * *and such other material as may be required by the Court of Appeals*" (emphasis supplied).

3. Rule 183 requires clear error review within the Tax Court.

The Commissioner and the Tax Court have taken inconsistent and constantly shifting positions on the meaning of Rule 183. In this litigation, the Commissioner argued at the certiorari stage that the "due regard" and "presumed correct" standards in the Rule do not require the Tax Court to give any deference at all to the findings of the STJ. Cert. Opp. 15. But as the Commissioner now admits, the Tax Court itself stated at the time these terms were codified that they require the Tax Court to accord the STJ's findings "special weight insofar as those findings are determined by the opportunity to hear and observe the witnesses." IRS Br. 27.

In a thorough analysis of the well-established plain meaning of the terms "presumed correct" and "due regard," along with the history of the relevant rules, Judge Williams concluded in *Stone* that the "special weight" Rule 183 accords STJ findings permits the Tax Court to overturn those findings only when clearly erroneous. Kanter Br. 28-34. This Court in *Freytag* similarly observed that "deferential" review is required by the rule. 501 U.S. at 874 n.3. And this Court has equated presumptive correctness with clear error review. *Bose*, 466 U.S. at 500. See 1 Childress & Davis, STANDARDS OF REVIEW 28 n.12 (1986) ("Today in ordinary civil cases *presumptively correct* is presented as the flip-side to *clear error review* • • • and seems no different in practice or common meaning"). As Judge Williams explained, the Tax Court is not at liberty to abandon or rewrite this regulatory standard in the midst of a lawsuit to achieve an advantage in the appellate court. See *supra*, p. 6 (citing cases holding that regulations bind decisionmakers until amended or withdrawn). If the Tax Court disagreed with the D.C. Circuit's interpretation in *Stone*, the Tax Court could have amended Rule 183 to eliminate the "presumed correct" and "due regard" constraints. But the Tax Court has not changed these terms in the Rule in the 15 years since *Stone* was decided. Rule 183 thus continues to ameliorate the constitutional

problem addressed in *Raddatz* by respecting the unique capacity of the trial judge to engage in factfinding, particularly on matters of credibility, especially where, as Judge Cudahy noted, factfinding depends on assessing the interlocking testimony of over 60 witnesses who testified at a five-week trial. Combined with disclosure of the STJ report, the clear error standard assures a fair adjudication.

The Commissioner seeks to avoid this result by arguing that the Rule does not by its terms mandate service of the STJ report on the parties. As a result, the Commissioner asserts that the Rule does not require "any sort of appellate-style review." Br. 25. But this is another straw man. Petitioners do not argue that Rule 183 requires full appellate-style review. Petitioners argue only that the standard of review in the Rule requires that the Tax Court give "special weight" to the institutional position of the trial judge and overturn his recommended findings only if clearly erroneous. The Commissioner cites the Fifth Circuit's decision in *Freytag*, but there the complaint was that *too much deference* had been given to the STJ. Even the Fifth Circuit did not remotely suggest that no deference was due the STJ's findings. IRS Br. 27. The Commissioner does not propose any recognized legal standard to give operational content to the "special weight" obligation. As the D.C. Circuit rightly concluded, the proper standard is the familiar clearly-erroneous standard (which is little different than the substantial-evidence test). A less deferential standard would clash with the plain language of the Rule, the Tax Court's own pronouncements, and the due process concerns expressed in *Raddatz*.

4. Congress has made the STJ report a public record that may not be suppressed.

A specific disclosure provision in the Internal Revenue Code, 26 U.S.C. 7461(a) makes "all reports of the Tax Court" and "all evidence received by the Tax Court" public records. In twice using the word "all," Congress chose broad language, consistent with its objective of making tax pro-

ceedings fully transparent in every respect. The word "of" signifies simply that the report must originate from the Tax Court; it does not require that the report come from a particular judge within it. BLACK'S LAW DICTIONARY 1080 (1990). Whether the Rule 183 report submitted by the STJ is "adopted" by the Tax Court, "modified" by the Tax Court, or "rejected" by the Tax Court, it is still a report of the Tax Court. And as Judge Cudahy concluded, this statute should be construed to avoid serious constitutional problems. Pet. App. 96a. It should also be construed in harmony with Congress's purpose to ensure transparency and fairness at every stage of tax proceedings. See Kanter Br. 46-49.

Congress understood that conflicts over taxation were of exceptional political significance and that public confidence in the taxation system requires complete transparency of all tax proceedings. The history of these provisions reveals why Congress did not require disclosure only of final judgments, but of "all" evidence, "all reports," and "all" findings of fact in tax proceedings. See 26 U.S.C. 7459(b). The Tax Court must disclose the entire stenographer's report, all the documentary evidence, and "all" reports of its judges. As Senator Jones said in proposing this legislation: "whenever there is a controversy between the Government and a taxpayer • • •, the proceedings leading up to that decision should be public proceedings • • • so that we may understand the facts upon which decisions are reached." 65 CONG. REC. 8132-8134 (1924).

The Commissioner does not dispute that, if the STJ's report is not an internal deliberative document, it would have to be made available to the litigants and the public under the centuries-old common law presumption of access to judicial documents. But as demonstrated earlier, the Rule 183 report cannot be an internal deliberative document because, by law, its recommended findings are required to have legally operative weight in the Tax Court's decision. In enacting these disclosure statutes, Congress legislated against the backdrop of the familiar common-law right of access and paraphrased

that right and its justifications throughout the legislative debates. If a court considers a document in making its decision, the litigants and the public are entitled to review it.

This interpretation presents no anomalous consequences of the kind suggested (Br. 45) by the IRS. The Tax Court is free to print its STJ reports, as most tribunals do, but the language of 26 U.S.C. 7462 does not dictate the manner of disclosure. It leaves the Tax Court discretion in such matters. Of course, 26 U.S.C. 7459 requires that final decision be made "in accordance" with the report as adopted or modified by the Tax Court, not a rejected report of the STJ. But none of this suggests that the STJ report may be suppressed.

Avoidance of constitutional decisionmaking weighs in favor of a construction of this law that requires production of STJ reports. *DeBartolo*, 485 U.S. at 575. Congress has also given this Court rule-making power over all appeals arising from the Tax Court (26 U.S.C. 7482(c)(2)) and has required transparency in the clearest possible language. As Professor Lederman explains, the Tax Court's authority over its own proceedings does not include improperly truncating the record to be reviewed in the Courts of Appeals. Br. 19-22.

5. Disclosure of the STJ report is needed to guard against the risk of serious injustice in this case.

Judge Couvillion had ample reason to conclude that the IRS failed to prove underpayment of taxes or fraud in this case. Kanter Br. App. 6a; JA 16-22. Although the centerpiece of the IRS's case against petitioners was a claim that they received "kickbacks" (IRS Br. 4-5), each and every witness called by the government denied that kickbacks were paid or that improper "influence" was ever exercised. See, *e.g.*, JA 11-16. Although the IRS complained of a "complex network of corporations" used to "launder" these purported kickbacks (IRS Br. 5), the Tax Court since has made clear that "the Court did not hold" that these corporations were "a sham to be disregarded for tax purposes." *Investment Research Associates* v. *Comm'r*, No. 43966-85, Feb. 21, 2001 Order, at 1. The revenues at issue in this litigation were paid

to these same corporations and reported on their income tax returns, a fact never disputed by the IRS. Those revenues flowed from the investment of corporate funds and were not taxable individually to Kanter or Ballard.*

Two of the IRS revenue agents who examined this case accordingly concluded: "No intent to defraud was found per this agent and the prior agents' exam, discussions with involved parties and professional judgment." Tr. 3184-3186, 3194-3200, 3202-3209; Exs. 9056-9058 PBL. Judge Couvillion, after reviewing thousands of exhibits and hearing from over 60 witnesses, agreed with these IRS agents' assessment. Kanter Br. App. 6a. That conclusion was reached after four years of study of the record and is supported by the Fifth Circuit's finding that there was no clear and convincing evidence of fraud in the appeal of taxpayer Lisle. *Lisle* v. *Comm'r*, 341 F.3d 364. Judge Dawson overturned the findings set forth in the Rule 183 report without mentioning or acknowledging them. The result is that a tax practitioner and prominent businessman have been branded as fraudfeasors, exposed to a demand for $30 million (most of which consists of penalties for fraud), and stripped of professional and business opportunities they formerly enjoyed. The Rule 183 report is sorely needed by the appellate courts to do justice to these citizens.

CONCLUSION

The decisions of the Seventh and Eleventh Circuits should be reversed.

Respectfully submitted.

---

* During the years in question, petitioner Ballard paid over $6 million in federal income taxes. Petitioner Kanter paid self-employment taxes but no income taxes because he suffered large investment losses.

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Supreme Court of the United States

CLAUDE M. BALLARD, ET UX.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ESTATE OF BURTON W. KANTER, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Writ Of Certiorari To The United States Courts Of Appeals For The Seventh And Eleventh Circuits

BRIEF OF *AMICA CURIAE* PROFESSOR LEANDRA LEDERMAN IN SUPPORT OF PETITIONERS

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INTEREST OF THE *AMICA CURIAE*

Amica is a professor of tax law with a long-standing interest in the operation of the United States Tax Court ("Tax Court") and its role in the federal system. She has written extensively on tax procedure, with an emphasis on issues relating to the Tax Court. She is co-author of *Tax Controversies: Practice and Procedure* (2d ed. 2002) and served as General Editor of *Federal Tax Practice and Procedure* (2003).[1]

SUMMARY OF THE ARGUMENT

One of the questions in this case is whether the Tax Court effectively can shield from appellate review the work of its Special Trial Judges in the largest cases over which those judges preside, cases heard under Tax Court Rule 183. Internal Revenue Code § 7482(a) provides, in relevant part, that "[t]he United States Courts of Appeals . . . shall have exclusive jurisdiction to review the decisions of the Tax Court . . . in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury . . . ." I.R.C. § 7482(a)(1). The Tax Court's current practice of keeping the reports of Special

[1] Pursuant to this Court's Rule 37.3(a), *amica curiae* is filing this brief with the written consents of all of the parties, which are being submitted with this brief. Pursuant to this Court's Rule 37.6, *amica* states that this brief was not authored in whole or in part by counsel for any party. *Amica* received no monetary contribution to the preparation or submission of this brief apart from the general financial support of the two academic institutions with which she is affiliated. The views expressed in this brief are those of *amica* and do not necessarily reflect the views of either institution.

Trial Judges in Rule 183 cases out of the record on appeal violates this statute because it renders the United States Courts of Appeals incapable of reviewing Tax Court decisions "to the same extent" as bench trials in the district courts.

ARGUMENT

In the Tax Court trial that gave rise to this appeal, the court assigned one of its Special Trial Judges ("STJs") to try the case. *See Investment Research Assoc. v. Commissioner*, 78 T.C.M. (CCH) 951 (1999) (Tax Court opinion below, reflecting assignment to Special Trial Judge D. Irvin Couvillion). STJs are inferior officers of the United States. *Freytag v. Commissioner*, 501 U.S. 868, 881-82 (1991). By statute, the Chief Judge of the Tax Court is authorized to assign to STJs any Tax Court proceeding, I.R.C. § 7443A(b), but the STJ may not "make the decision of the court" in cases in which more than $50,000 is placed in dispute, I.R.C. § 7443A(c); *see also Freytag*, 501 U.S. at 875 n.3.

In Tax Court Rule 183, the Tax Court has prescribed procedures for the conduct of these large cases. *See* Tax Ct. R. 183. Under that rule, the STJ conducts the trial, after which, the parties submit briefs. Tax Ct. R. 183(a). Rule 183 also provides that "[a]fter all the briefs have been filed by all the parties or the time for doing so has expired, *the Special Trial Judge shall submit a report, including findings of fact and opinion*, to the Chief Judge . . . ." Tax Ct. R. 183(b) (emphasis added). Thus, in a large case heard by a STJ, it is the STJ who makes findings of fact and

writes an opinion, both of which are reflected in a report submitted to the Chief Judge of the Tax Court.

Tax Court Rule 183 further mandates that *"[d]ue regard* shall be given to the circumstance that the *Special Trial Judge had the opportunity to evaluate the credibility of witnesses,* and the *findings of fact recommended by the Special Trial Judge shall be presumed to be correct."* Tax Ct. R. 183(c) (emphasis added). Yet, the Tax Court's current practice is to shield the STJ's report from the eyes and oversight of even a reviewing Court of Appeals. *See* Leandra Lederman, *Transparency and Obfuscation in Tax Court Procedure*, 102 Tax Notes 1539, 1540 (Mar. 22, 2004).

The Tax Court's current practice of keeping STJ reports confidential reflects a change from its prior procedure; through 1983, the applicable Tax Court rule both expressly required a copy of the STJ's report to be served on each party and provided the parties with an opportunity to file exceptions to the report. *See* Tax Ct. R. 182(b), (c), 60 T.C. 1149 (1973) (repealed 1984). "There is no public indication why the Tax Court rules and procedures were changed in 1983 to the current system . . . ." *Estate of Kanter v. Commissioner*, 337 F.3d 833, 879 (7th Cir. 2003) (Cudahy, J., concurring in part and dissenting in part). Moreover, this "abandon[ment] [of] a transparent process" reflects "an evolution completely counter to the trend towards transparency in analogous areas of the law." *Id.*

The Tax Court is a creature of statute, see I.R.C. § 7441, and Congress has provided that "[t]he Tax Court and its divisions shall have such jurisdiction as is conferred on them by this title [and other specified statutes]." I.R.C. § 7442. Congress has delegated to the Tax Court the task of promulgating rules of practice and procedure for

the conduct of its proceedings, both generally and with respect to STJs. *See* I.R.C. §§ 7443A(a), 7453. However, the Tax Court does not write its rules in a vacuum. "[The Tax Court's] authority under 26 U.S.C. § 7453 . . . is limited to maintaining control over the court's own docket and proceedings." *Daccarett-Ghia v. Commissioner*, 70 F.3d 621, 625 (D.C. Cir. 1995); *cf. Board of Tax Appeals v. United States*, 37 F.2d 442, 443 (D.C. Cir. 1929) ("The Commissioner . . . must be given an opportunity to be heard, and no rule of the Board [of Tax Appeals] can deprive him of the statutory right thus conferred.").

Sections 7443A and 7453 of the Internal Revenue Code do not grant the Tax Court the authority to regulate the conduct of other courts, such as the Courts of Appeals. Congress has specifically provided that "[r]ules for review of decisions of the Tax Court shall be those prescribed by the Supreme Court under section 2072 of Title 28 of the United States Code." I.R.C. § 7482(c)(2). Thus, Tax Court rules, such as Rule 183, cannot determine how the Courts of Appeals review decisions of the Tax Court and should not be interpreted so as to limit the scope of that review.[2] Instead, rules that this Court has promulgated under 28 U.S.C. § 2072 and applicable federal statutes must govern that review.

The key statute governing review of Tax Court decisions is § 7482. It provides the United States Courts of Appeals with jurisdiction to review decisions of the Tax

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[2] Current Tax Court Rule 183 does not forbid disclosure of the STJ's report; the provisions mandating that disclosure were removed but not replaced with any prohibition of the prior practice. *See* Tax Ct. R. 183 & note on amendments to rule, 81 T.C. 1069-70 (1983).

Court "*in the same manner and to the same extent as decisions of the district courts* in civil actions tried without a jury . . . ." I.R.C. § 7482(a)(1) (emphasis added). As discussed below, this statute requires the STJ's report to be included in the record on appeal, both because that report cannot otherwise be accorded the weight required by law and because, in district court, the original findings of fact and opinion are included in the record on appeal, even if those findings and opinion are those of a judicial officer rather than a judge.

I. THE SPECIAL TRIAL JUDGE'S REPORT MUST BE INCLUDED IN THE RECORD ON APPEAL IN ORDER FOR THE ORIGINAL FINDINGS OF FACT OF THE TRIAL JUDGE TO RECEIVE THE REVIEW REQUIRED BY LAW

This Court has interpreted § 7482(a)(1) as requiring Tax Court decisions to receive the same standard of review as district court decisions, so that Federal Rule of Civil Procedure 52(a) applies to review of Tax Court decisions. *See Commissioner v. Duberstein*, 363 U.S. 278, 291 & n.13 (1960) (*citing Grace Bros., Inc. v. Commissioner*, 173 F.2d 170, 173 (9th Cir. 1949)). Federal Rule of Civil Procedure 52(a) provides, in part that "[f]indings of fact, whether based on oral or documentary evidence, shall not be set aside unless clearly erroneous, and *due regard shall be given to the opportunity of the trial court to judge of the credibility of the witnesses*." Fed. R. Civ. P. 52(a). Thus, in Tax Court, as in district court, findings of fact are subject to review on appeal and the appellate court must give "due regard" to the trial court's opportunity to observe the witnesses and thereby make credibility assessments.

In Rule 183 cases, it is the STJ who is the original finder of fact and who observes the witnesses. In order for the due regard and clearly erroneous standards of Federal Rule of Civil Procedure 52(a) to be complied with, the STJ's report must be included in the record on appeal. Otherwise, the Courts of Appeals could be put in the untenable position of unwittingly upholding, as not clearly erroneous, findings that were not those of the trial judge. Similarly, the Courts of Appeals could unwittingly respect credibility determinations that were not those of the judge who observed the witnesses.

> If the appellate judges who review for correctness are denied information they would otherwise consider, if information is transmitted to them in a form which inhibits full perception of an important aspect of the case, or if the information is skewed, even the best-focused scrutiny will be misdirected and the most genuine consensus may rest on this misconception.

Robert S. Thompson & John B. Oakley, *From Information to Opinion in Appellate Courts: How Funny Things Happen on the Way Through the Forum*, 1986 Ariz. St. L.J. 1, 11 (1986); *cf. Dayton Board of Education v. Brinkman*, 443 U.S. 526, 534 n.8 (1979) (agreeing with dissenting Justice Stewart "that there is great value in appellate courts showing deference to the fact-finding of local trial judges.").

In addition, any approach other than including the STJ's report in the record on appeal would lead to different types of review under Federal Rule of Civil Procedure 52(a) depending on whether a Tax Court judge or STJ is the trier of fact. That is, if a Tax Court judge hears the case, the Court of Appeals will have in the record the

findings of fact of the trier of fact and can uphold them unless clearly erroneous and give due regard to that judge's opportunity to observe the witnesses. By contrast, if the STJ's report in a large case is not included in the record on appeal, the original findings of fact and credibility determinations of the STJ will not be available to the Court of Appeals.

This is not an infrequent issue, given that Judge Cudahy found over 880 Tax Court decisions since 1983 that involved a STJ report. *See Estate of Kanter*, 337 F.3d 833, 876 (7th Cir. 2003) (Cudahy, J., concurring in part and dissenting in part). In addition, STJs may be assigned large cases that are very fact-intensive. *See Freytag v. Commissioner*, 501 U.S. 868, 872 n.1 (1991) (describing the case as one that "involved one of the longest trials . . . in the tax court's history – 14 weeks of evidence, complex financial testimony, 9,000 pages of transcripts, 3,000-plus exhibits."). In fact, the Tax Court trial below, "consumed 28 days of trial time. There were 55 government witnesses. The transcript exceeded 5,000 pages." Cornish F. Hitchcock, *Public Access to Special Trial Judge Reports*, 93 Tax Notes 403, 404 (Oct. 15, 2001). Furthermore, it is the Chief Judge of the Tax Court who decides which large cases to assign to STJs, I.R.C. § 7443A(b), so the selection of cases for this procedure is not random. Assignment also is not subject to party consent. Given this context, a system that shields from Court of Appeals review the initial fact-finding in large cases presided over by STJs provides an unhealthy incentive for the assignment to STJs of controversial or fact-intensive cases.

Furthermore, Tax Court Rule 183 has its own "due regard" provision, applicable to the Tax Court. It provides that "[d]ue regard shall be given to the circumstance that

the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Tax Ct. R. 183(c). In order for this rule to be enforceable, the STJ's report must be included in the record on appeal.

As this Court has stated:

> the trial on the merits should be "the 'main event' . . . rather than a 'tryout on the road.'" *Wainwright v. Sykes*, 433 U.S. 72, 90 (1977). For these reasons, review of factual findings under the clearly-erroneous standard – with its *deference to the trier of fact* – is the rule, not the exception.
>
> When findings are based on determinations regarding the *credibility of witnesses, Rule 52(a) demands even greater deference to the trial court's findings*; for only the trial judge can be aware of the variations in demeanor and tone of voice that bear so heavily on the listener's understanding of and belief in what is said.

Anderson v. Bessemer City, 470 U.S. 564, 575 (1985) (emphasis added). The only way for a Court of Appeals to accord *any* deference at all to the findings of fact and credibility determinations of the trial judge in a Rule 183 case – or to evaluate whether the Tax Court has given proper regard to the STJ's position as trier of fact under its own rule – is for the STJ's report to be included in the record on appeal.

II. BECAUSE CONGRESS HAS PROVIDED FOR REVIEW OF TAX COURT DECISIONS TO THE SAME EXTENT AS DISTRICT COURT DECISIONS AND BECAUSE THE RECORD ON APPEAL IS A CRITICAL PART OF THAT REVIEW, THE FINDINGS OF FACT AND CONCLUSIONS OF THE TRIAL JUDGE, WHICH WOULD BE INCLUDED IN THE RECORD ON APPEAL OF A DISTRICT COURT TRIAL WITHOUT A JURY, CANNOT BE EXCLUDED FROM THE RECORD ON APPEAL OF A TAX COURT CASE

As noted above, § 7482(a) provides, in relevant part, that "[t]he United States Courts of Appeals . . . shall have exclusive jurisdiction to review the decisions of the Tax Court . . . in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury . . . ." I.R.C. § 7482(a)(1). This section was enacted in 1948 to overturn the holding of *Dobson v. Commissioner*, 320 U.S. 489 (1943), which had interpreted then-existing law, including the predecessor of § 7482(c)(1), as allowing only limited review of Tax Court decisions. *See* S. Rep. No. 80-1559, at 13 (1948); Harold Dubroff, *The United States Tax Court: An Historical Analysis* 381-82, 386 (1979).

The history of § 7482(a)(1) reflects Congress' intent to provide for appellate review of Tax Court (then Board of Tax Appeals) decisions that was no more limited than review of district court decisions, at least on questions of fact. A Senate Report refers to the provision as repealing the *Dobson* rule and thereby "mak[ing] decisions of the Tax Court on questions of fact reviewable if clearly

erroneous, as is now the case with similar decisions of the district courts," S. Rep. No. 80-1559, at 13 (1948), while the Committee on the Judiciary spoke more broadly:[3]

> From the time . . . appellate review [of Tax Court decisions] was established by the Revenue Act of 1926 until the *Dobson* decision in 1943, there had been no suggestion that the review of the Tax Court decisions was any more limited than the appellate review of decisions of the United States District Courts. . . . The Supreme Court in the *Dobson* case, however, created a new rule of law which would not permit even law questions to be reviewed unless they were clear-cut questions of law, and which would not permit any worth-while review of decisions of fact. . . .
>
> [The provision in the Senate bill] *restores to the circuit courts of appeal the power to review cases from the Tax Court in the same manner and to the same extent as it has power to review other cases* – whether tax cases or nontax cases

---

[3] In part because of ambiguity in the legislative history and in part because Congress retained the language of what is now § 7482(c)(1), which empowers a Court of Appeals to modify or reverse the Tax Court's decision if it "is not in accordance with law," there has been academic commentary to the effect that "[a]t a minimum . . . the language and history of the 1948 amendment leave the door open for the courts to construe the amendment as limited to providing a new standard for review of factual issues ('clearly erroneous') while retaining the *Dobson* standard for legal issues (entitled to 'great deference')." David F. Shores, *Deferential Review of Tax Court Decisions:* Dobson *Revisited*, 49 Tax Law. 629, 653 (1996). Nonetheless, "[f]or approximately the last 50 years, Tax Court decisions on questions of law have been subject to de novo review by the court[s] of appeals . . . ." David F. Shores, *Deferential Review of Tax Court Decisions: Taking Institutional Choice Seriously*, 55 Tax Law. 667, 667 (2002).

> – coming from a District Court in a case tried without a jury.

Views of the Committee on the Judiciary with Respect to Senate Amendments to H.R. 3214, reprinted in 94 Cong. Rec. 8501 (1948) (emphasis added); *see also Commissioner v. Duberstein*, 363 U.S. 278, 291 n.13 (1960) ("The purpose of the 1948 legislation was to remove from the law the favored position (in comparison with District Court and Court of Claims rulings in tax matters) enjoyed by the Tax Court under this Court's ruling in *Dobson v. Commissioner*, 320 U.S. 489.").

As the history of § 7482(a)(1) shows, it is a provision with substantive content. It is intended to provide both for meaningful appellate review of Tax Court decisions and for a particular kind of appellate review – review comparable to that afforded decisions in civil bench trials in district court, particularly on factual questions. In fact, this Court has cited § 7482(a) as requiring application of the "clearly erroneous" standard of review of Federal Rule of Civil Procedure 52(a) on appeal from Tax Court decisions, *Duberstein*, 363 U.S. at 291 & n.13, as discussed above, and in support of the important principle that "[t]he Tax Court's function and role in the federal judicial scheme closely resemble those of the federal district courts," *Freytag v. Commissioner*, 501 U.S. 868, 891 (1991).

A. The Contents of the Record on Appeal are Key for Appellate Review

Appellate review of the decision of a trial court is based on the record on appeal. *See* 20 *Moore's Federal Practice* § 310.02[1] (3d. ed. 1997) ("The contents of the

record as it is presented to the circuit court determine and limit the issues that may be addressed on appeal."); Cora M. Thompson, *Cyclopedia of Federal Procedure* § 61.02 (rev. 3d ed. 1994) ("A written or printed record is the basis of all ordinary modes of review by a higher court. Barring matters of which the court may take judicial notice, consideration of the court of review is confined to the record which is filed in the particular case.") (footnotes omitted); *Abatino v. United States*, 750 F.2d 1442, 1445 (9th Cir. 1985) ("The Court of Appeals' review of a District Court's order must be made on the basis of the record on appeal, which comes up from the district court.").

Thus, the contents of the record on appeal determine the parameters of appellate review. *Cf. Jackson v. United States*, 131 F.2d 606, 607 (8th Cir. 1942) ("In addition to the record on appeal, we have been furnished by the Government with certain documents explanatory of what occurred in the court below. We cannot, of course, concern ourselves with anything which does not appear in the record."); *cf. Hughes v. Wendel*, 317 U.S. 134, 134 (1942) (*per curiam*) (dismissing appeal where "[t]he record . . . [did] not set forth appellant's lease, and the incomplete summary of it contained in her pleading [was] not adequate to enable [the Court] to determine what her rights may be."); *James Petroleum Corp. v. Commissioner*, 331 F.2d 344, 346 (10th Cir. 1964) ("The Internal Revenue Code of 1954, § 7482, states that the Court of Appeals shall review the decisions of the Tax Court in the same manner and to the same extent as the decisions of the District Courts. This requires complete findings of fact to demonstrate the basis for decision.").

> The appeal record is virtually as old as the appellate process itself. Unless the appellate court is

> to act de novo and disregard all that went on in the trial court, *it is essential that the appellate court be able to determine what occurred in the trial court.* This is particularly important when the purpose of appellate review is, as it is in most appeals, error correction . . . .
>
> The effect of [various rules regarding the record] is to make *the record on appeal crucial to the appellate process.*

Robert J. Martineau, *Modern Appellate Practice: Federal and State Civil Appeals* § 8.1 (1983) (footnotes omitted); *cf. Commissioner v. McCoy*, 484 U.S. 3, 6 (1987) (citing § 7482(a) and (c)(1) and stating, "[i]t follows that in reviewing a Tax Court decision, the duty of the court of appeals is to consider whether the Tax Court committed error.").

Because of the key role of the record on appeal in appellate review, for Tax Court decisions to be afforded the review required by § 7482(a)(1), a document that would be part of the record on appeal of a district court bench trial must be included in the record on appeal of a Tax Court case. Moreover, the Federal Rules of Appellate Procedure provide that *the same rule providing the content of the record on appeal in District Court cases applies to appeals from the Tax Court. See* Fed. R. App. P. 13(d)(1) (providing, in part, that Rule 10, relating to the record on appeal, applies to appeals from Tax Court cases and that "[r]eferences in [that rule] . . . to the district court and district clerk are to be read as referring to the Tax Court and its clerk.").

B. The Record on Appeal from a District Court Case Includes the Original Findings of Fact, Including Those of an Inferior Officer who Heard a Dispositive Matter or Conducted the Trial

Federal Rule of Appellate Procedure 10(a) provides a list of the items that constitute the record on appeal in a district court case:

> (1) the original papers and exhibits filed in the district court;
>
> (2) the transcript of proceedings, if any; and
>
> (3) a certified copy of the docket entries prepared by the district clerk.

Fed R. App. P. 10(a).[4]

> The first part, *original papers, is broadly defined* to include all documents filed with, and presented to, the district court. *The term includes documents presented and filed, whether by a party or by the district judge.* . . . Examples of documents that are classified as original papers include: . . .
>
> – court memoranda . . . ;

---

[4] Federal Rule of Appellate Procedure 10 also authorizes a truthful agreed statement of the parties "showing how the issues presented by the appeal arose and were decided in the district court. . . . together with any additions that the district court may consider necessary to a full presentation of the issues on appeal . . . approved by the district court and . . . certified to the court of appeals as the record on appeal" to be substituted for the record on appeal defined in Rule 10(a). Fed. R. App. P. 10(d).

> – master's reports . . . ;
>
> – findings of fact and conclusions of law;
>
> – opinions of the court; [and]
>
> – judgments . . . .

20 *Moore's Federal Practice* § 310.10[1] (3d. ed. 1997) (emphasis altered) (footnotes omitted).

Thus, in district court, not only are papers filed by the parties included in the record on appeal, but documents filed by the court – such as memoranda, findings of fact, reports, and opinions – are included as well. *See, e.g., Brown v. United States*, 277 F.2d 201, 202 (8th Cir. 1960) ("detailed memorandum" written by the judge was one of the "original papers of the District Court" and was furnished to Court of Appeals); *United States v. Certain Interests in Property*, 296 F.2d 264, 268 (4th Cir. 1961) (quoting from "unreported statement of . . . findings of fact and conclusions" prepared by district court judge in addition to his reported opinion).

> Even the Commissioner, at oral argument [in *Estate of Kanter*], acknowledged that in *every milieu except that of the Tax Court, the document containing the findings or recommendations of the official conducting the trial are available to a court reviewing the operative decision.* This includes, for example, the report of a federal magistrate judge to a district court responsible for a decision.

Estate of Kanter v. Commissioner, 337 F.3d 833, 874 (7th Cir. 2003) (Cudahy, J., concurring in part and dissenting in part) (emphasis added).

Tax Court STJs are analogous to magistrate judges; in district court, magistrate judges may make findings and recommendations, as well as conduct trials. *See Estate of Smith v. Commissioner*, 638 F.2d 665, 669 (3d Cir. 1981) ("As we see it, the special trial judge acts in a capacity not dissimilar to that of a magistrate in district court."). "[M]agistrate judges and special trial judges enjoy the same constitutional status as 'inferior officers.'" Kathleen Pakenham, *You Better Shop Around: The Status and Authority of Specialty Trial Judges in Federal Tax Cases*, 103 Tax Notes 1527, 1532 (June 21, 2004).

Although district court magistrate judges may be assigned a variety of matters, *see* 28 U.S.C. § 636, nonconsensual district court use of magistrate judges in "dispositive" pretrial matters (those encompassed by 28 U.S.C. § 636(b)(1)(B)) is most analogous to the Tax Court's use of STJs in Rule 183 cases because, in those matters, as in Rule 183 cases, (1) the judicial officer (magistrate or STJ) presides over proceedings that may dispose of the case; (2) consent of the parties is not required for the assignment of the magistrate or STJ to the matter; and (3) the magistrate or STJ makes a recommendation to a judge, not a decision. *Compare* Tax Ct. R. 183 *with* 28 U.S.C. § 636(b)(1). In addition, a magistrate's report and recommendation on a dispositive matter is analogous to a STJ's report under Rule 183. *See Klein v. United States*, 94 F. Supp. 2d 838, 847 (E.D. Mich. 2000) ("Like a federal magistrate judge's report and recommendation to the district court, a Special Trial Judge's proposed findings and opinion become those of the Tax Court once adopted by the presiding Tax Court judge.") (*citing Freytag*, 501 U.S. at 873); *cf. Estate of Kanter*, 337 F.3d at 874 (Cudahy, J., concurring in part and dissenting in part) (referring by analogy in Tax Court

Rule 183 case to "the report of a federal magistrate judge to a district court responsible for a decision.").

The magistrate's report and recommendation in a dispositive matter are included in the record on appeal. In dispositive matters, "the magistrate shall *file his proposed findings and recommendations . . . with the court . . . .*" 28 U.S.C. § 636(b)(1)(C) (emphasis added). Documents filed with the court constitute part of the record on appeal under Federal Rule of Appellate Procedure 10. *See* Fed. R. App. P. 10(a)(1). Federal Rule of Civil Procedure 72 adds that in dispositive pretrial matters heard by a magistrate without consent of the parties, "[a] record shall be made of all evidentiary proceedings before the magistrate judge, and a record may be made of such other proceedings as the magistrate judge deems necessary. The magistrate judge shall *enter into the record* a recommendation for disposition of the matter, including proposed findings of fact when appropriate." Fed. R. Civ. P. 72(b) (emphasis added).

Of course, in Rule 183 cases in Tax Court, the STJ may conduct the entire trial. *See* Tax Ct. R. 183(a). In those cases in which a magistrate judge conducts a district court trial (by consent of the parties) and enters judgment, "an aggrieved party may appeal directly to the appropriate United States court of appeals from the judgment of the magistrate in the same manner as an appeal from any other judgment of a district court." 28 U.S.C. § 636(c)(3); *see also Roell v. Withrow*, 538 U.S. 580, 585 (2003); Fed. R. Civ. P. 73(c). "When functioning in this capacity, magistrate judges are appropriately viewed as proxies for district judges . . . ." A.J. Stephani & Glen Weissenberger, *Federal Civil Procedure 2003 Litigation Manual* 536 (2002). No other judge need be involved in the case at the district court level, so the magistrate judge's findings are

necessarily those subject to review on appeal and Federal Rule of Appellate Procedure 10(a) should apply to determine the contents of the record on appeal, just as it does in other district court cases. *See* Fed. R. App. P. 10(a); *see also Madison v. Parker*, 104 F.3d 765, 767 (5th Cir. 1997) ("We review a judgment rendered by a magistrate judge just as we do a judgment rendered by a district judge.") (*citing* 28 U.S.C. § 636(c)(3)).

Thus, in district court, original findings of fact, including those of magistrate judges, who are analogous to STJs, are included in the record on appeal. Judge Cudahy stated in his separate opinion in *Estate of Kanter*, "in every milieu except that of the Tax Court, the document containing the findings or recommendations of the official conducting the trial are available to a court reviewing the operative decision." *Estate of Kanter*, 337 F.3d at 874 (Cudahy, J., concurring in part and dissenting in part). Most importantly, "[t]his includes . . . the report of a federal magistrate judge to a district court responsible for a decision." *Id.* (Cudahy, J., concurring in part and dissenting in part). Given the similarities between the district court's report and recommendation procedure and the Tax Court's procedure in Rule 183 cases, the omission of the STJ's report from the record on appeal violates § 7482 because it prevents appellate review of the Tax Court decisions "to the same extent as decisions of the district courts in civil actions tried without a jury," I.R.C. § 7482(a)(1).

C. Like the District Courts, the Tax Court Cannot Opt to Omit Case Documents from the Record on Appeal

"[U]nder [Federal] Rule [of Appellate Procedure] 10(a), all of the original papers and exhibits filed in the district court are a part of the record on appeal whether or not brought before [the appellate] court." *Chapman v. Rudd Paint & Varnish Co.*, 409 F.2d 635, 638 (9th Cir. 1969). "[A]s a matter of law the district court's record now constitutes the record on appeal." David G. Knibb, *Federal Court of Appeals Manual* § 27.1 (3d ed. 1997). Moreover, "[i]t is not the type of paper submitted but rather the fact of filing which determines whether a particular item will be included in the record." *International Business Machines Corp. v. Edelstein*, 526 F.2d 37, 45 (2d Cir. 1975).

Because the fact of filing a document with the court is the linchpin of inclusion in the record on appeal under Federal Rule of Appellate Procedure 10(a), a court's refusal to file a document raises an issue of usurpation of power. *See id.* In *International Business Machines Corp.*, the Court of Appeals for the Second Circuit stated, "[t]he [trial] judge's refusal to file IBM's papers . . . raise[s] such issue [of usurpation of power], because the *Petitioner is thereby prevented from making a record for purposes of appeal.*" *Id.* (emphasis added).

The court added:

> The policy that it is the appealing parties, and not the trial court, who control the issues to be presented on appeal has been embodied in federal practice since the Federal Rules were adopted in 1938. . . .

> On the basis of this policy, *district courts have refrained from exercising any degree of control over the contents of the trial record*, . . . even where parties have petitioned the trial court to exclude certain items from the record.

Id. at 45-46. The court therefore held:

> Since Petitioner has no other means of presenting its arguments to the appellate court – whether as appellant or appellee – save by making the necessary record at the trial level, Judge Edelstein's refusal to file petitioner's motions has constituted an *impermissible interference with petitioner's right to make the record it chooses for purposes of appeal.*

Id. at 46; *cf. United States v. Forness*, 125 F.2d 928, 932 (2d Cir. 1942) (interpreting prior Federal Rule of Civil Procedure 75(h), which governed the record on appeal, as precluding the district court judge from striking certain affidavits from the record, and finding that the rule "permit[ted] him only to add to the record, or to correct it.").

The policy reflected in the Second Circuit's opinion in *International Business Machines Corp.* applies with equal force to the Tax Court. Section 7482(a)(1) provides for review of Tax Court decisions to the same extent as review of district court decisions, and, as explained above, the record on appeal is the linchpin of that review. Furthermore, Federal Rule of Appellate Procedure 10, which was applied in *International Business Machines Corp.*, applies to the Tax Court, as well. *See* Fed. R. App. P. 13(d)(1).

Thus, the Tax Court should not be able to refuse to file a document, so as to make it part of the record, any more

than a district court can. Yet, the Tax Court has done the practical equivalent of that. The Tax Court previously provided complete transparency in cases heard under Rule 183, including service of a copy of the STJ's report on each party and an opportunity to file exceptions to the report with respect to both fact and law. *See* Tax Ct. R. 182(b), (c), 60 T.C. 1149 (1973) (repealed 1984). The prior Tax Court rule also required the STJ to *file* his report, *see id.*, which resulted in its inclusion in the record on appeal under the Federal Rules of Appellate Procedure. *See* Leandra Lederman, *Transparency and Obfuscation in Tax Court Procedure*, 102 Tax Notes 1539, 1540 & n.10 (Mar. 22, 2004).

In 1983, the Tax Court amended its rule without indicating that there were any problems under the existing procedure or otherwise explaining its motivation. *See* Tax Ct. R. 183 note on amendments to rule, 81 T.C. 1069-70 (1983) (amending and renumbering former Rule 182). All that the 1983 note to Rule 183 states with respect to this change is:

> The prior provisions for service of the Special Trial Judge's report on each party and for the filing of exceptions to that report have been deleted. The prior provision for oral argument upon a motion of a party also has been deleted. However, par. (c) provides that the Division to which the case is assigned may direct the filing of additional briefs, receive further evidence, or direct oral argument.

Id., 81 T.C. 1070 (1983).

> There is no public indication why the Tax Court rules and procedures were changed in 1983 to the current system that disadvantages those appealing Tax Court decisions. And, of course, an

> appellate-style procedure such as that typical in all other areas of federal administrative adjudication would facilitate challenges, whether made by the taxpayer or by the Commissioner. The previous procedure may well have been abrogated for exactly this reason.

Estate of Kanter, 337 F.3d at 879 (Cudahy, J., concurring in part and dissenting in part). Given the requirements of § 7482(a)(1), the Tax Court cannot choose to omit from the record on appeal a document, such as the original findings of fact of the trial judge, that would be part of the record on appeal in a district court case.

III. INCLUSION OF THE SPECIAL TRIAL JUDGE'S REPORT IN A TAX COURT RULE 183 CASE IN THE RECORD ON APPEAL IS CONSISTENT WITH THE POLICY OF TRANSPARENCY CONGRESS MANIFESTED WHEN IT CREATED THE BOARD OF TAX APPEALS

In creating the predecessor of the Tax Court, the Board of Tax Appeals, Congress focused on a desire for transparency in its proceedings. For example, one Representative stated:

> I believe that the publicity features as contained in the bill are wholesome, are necessary, and while it may cause embarrassment and inconvenience, perhaps, to an individual here and there, it is for the good of all the taxpayers . . . . No fault can seriously be found in a provision which requires the proceedings of the board of appeals to be public. Let us be frank about that. . . . *The board of appeals and the publicity placed upon its activities are the result of a*

> *vicious secrecy system which has grown up in the Treasury Department under the present law.*

65 Cong. Rec. 9549 (1924) (statement of Rep. LaGuardia) (emphasis added). Congress refused to countenance such secrecy when it created the Board of Tax Appeals; the statute creating the Board of Tax Appeals required publicity in the proceedings of the Board and publication of its reports. *See* Harold Dubroff, *The United States Tax Court: An Historical Analysis* 65 & n.96 (1979).

The policy Congress manifested in favor of transparency in Tax Court proceedings continues to be reflected in current law. *See* I.R.C. §§ 7458 ("Hearings before the Tax Court and its divisions shall be open to the public . . . ."); 7461(a) ("Except as provided in subsection (b), all reports of the Tax Court and all evidence received by the Tax Court and its divisions, . . . shall be public records open to the inspection of the public."). The Tax Court's practice in Rule 183 cases is inconsistent with that policy. Judge Cudahy has argued:

> The fact is that this entire process of the Tax Court [in Rule 183 cases] appears designed to extract the efficiencies involved in designating cases to be heard by STJs without having to bear any of the procedural costs traditionally associated with this kind of adjunct decision making (e.g., transparency). I do not believe that the STJ's ultimate assent to the final opinion of the Tax Court is protection enough to the parties.

Estate of Kanter v. Commissioner, 337 F.3d 833, 887-88 (7th Cir. 2003) (Cudahy, J., concurring in part and dissenting in part).

Moreover, the "vicious" nature of a secret system is that it enables its actors to avoid accountability for their actions. Appellate review is a critical part of that accountability.

> Assuming that a judge deciding a case – like anyone making a decision – would not relish the thought of being told that she was wrong, the possibility of having her decision reversed on appeal imposes a cost and becomes a consideration in rendering judgments. In theory, lower-court judges, as a result, would be more likely to choose outcomes solidly based on legal justifications traceable to past decisions or statutes. Thus, appellate review enhances the rationality of lower court decision making by introducing the prospect of institutional censure: certain judicial choices can be constrained by the fact that some options have already been ruled out, or are likely to be ruled out, by a higher court.

David Frisch, *Contractual Choice of Law and the Prudential Foundations of Appellate Review*, 56 Vand. L. Rev. 57, 85 (2003).

Furthermore, appellate oversight of Article I courts by Article III courts may be constitutionally required. The plurality opinion in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), stated, "when Congress assigns [public rights] matters to administrative agencies, or to legislative courts, it has generally provided, and we have suggested that it may be required to provide, for Art. III judicial review." *Id.* at 69 n.23 (*citing Atlas Roofing Co. v. Occupational Safety and Health Review Comm'n*, 430 U.S. 442, 455 n.13 (1977)). Professor Richard Fallon has argued, "the central claim of my appellate review theory [is thus]: adequately searching appellate

review of the judgments of legislative courts and administrative agencies is both necessary and sufficient to satisfy the requirements of article III." Richard H. Fallon, Jr., *Of Legislative Courts, Administrative Agencies, and Article III*, 101 Harv. L. Rev. 915, 918 (1988); *see also* Deborah A. Geier, *The Tax Court, Article III, and the Proposal Advanced by the Federal Courts Study Committee: A Study in Applied Constitutional Theory*, 76 Cornell L. Rev. 985, 1026-27 (1991) (arguing that "article III appellate review" of the decisions of a legislative court such as the Tax Court is necessary but not sufficient).

Omission of the STJ's report from the record on appeal is inconsistent with these policies of transparency, oversight, and accountability. In addition, keeping the report secret is inconsistent with Congress' intent to make Tax Court proceedings public. Furthermore, in a Rule 183 case in Tax Court, only the appellate courts can oversee the reviewing judge's actions on the STJ's report. Excluding the report from the record on appeal eliminates that oversight, thereby precluding meaningful appellate review by an Article III court. *See Estate of Kanter*, 337 F.3d at 888 (argument of Judge Cudahy that "by eventually making the STJ's report public (and part of the available record of the Tax Court on appeal), [the Court of Appeals] will have an opportunity to conduct meaningful appellate review.") (Cudahy, J., concurring in part and dissenting in part).

> The correct finding, as near as may be, of the facts of a law suit is fully as important as the application of the correct legal rules to the facts as found. An impeccably "right" legal rule applied to the "wrong" facts yields a decision which is as

> faulty as one which results from the application of the "wrong" legal rule to the "right" facts. . . .
>
> . . . As fact-finding is a human undertaking, it can, of course, never be perfect and infallible. For that very reason every effort should be made to render it as adequate as it humanly can be.

United States v. Forness, 125 F.2d 928, 942-43 (2d Cir. 1942) (footnotes omitted).

CONCLUSION

The judgments of the United States Courts of Appeals for the Seventh Circuit and the Eleventh Circuit should be vacated and the cases remanded so that the report of Special Trial Judge Couvillion can be included in the record on appeal.

Respectfully submitted,

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CLAUDE M. BALLARD, ET UX., *Petitioners*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

ESTATE OF BURTON W. KANTER, ET AL., *Petitioners*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*.

On Writs of Certiorari to the United States Courts of Appeals for the Seventh and Eleventh Circuits

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IN THE

Supreme Court of the United States

No. 03-184

CLAUDE M. BALLARD, ET UX.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

No. 03-1034

ESTATE OF BURTON W. KANTER, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Writs of Certiorari to the United States Courts of Appeals for the Seventh and Eleventh Circuits

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BRIEF AMICUS CURIAE OF THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

STATEMENT OF INTEREST OF AMICUS CURIAE[1]

The National Federation of Independent Business Legal Foundation ("NFIB Legal Foundation")—a nonprofit public interest law firm established to protect the rights of America's small business owners—is the legal arm of the National Federation of Independent Business ("NFIB"), the Nation's oldest and largest organization dedicated to representing the interests of small business owners throughout all 50 states. The approximately 600,000 NFIB members own a wide variety of small businesses, including family farms, neighborhood retailers, service companies, and technology manufacturers.

The secretive process employed by the Tax Court is of concern to the NFIB Legal Foundation and the members of the NFIB. That process, and the court of appeals decisions below upholding it, raise serious questions about the actual and perceived fairness of Tax Court adjudications and the ability of small businesses effectively to contest disputes over tax liability in that court. The NFIB Legal Foundation supports the simplification of the process for determining and complying with tax obligations. The Tax Court's secretive handling of STJ reports, however, makes the process for adjudicating tax disputes more complicated and less transparent.

The NFIB Legal Foundation, or the NFIB itself, has filed briefs *amicus curiae* in prior cases of this Court affecting the interests of small business owners at both the petition and merits stages. *See Walters* v. *Metropolitan Educ. Enters.*,

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[1] This brief was authored by Hogan & Hartson L.L.P., which serves as counsel for *amicus curiae* in this case. Pursuant to this Court's Rule 37.6, we note that Hogan & Hartson has represented the *Kanter* petitioners in other, non-litigation matters. Hogan & Hartson has not served as counsel for those parties in this case, however, and none of the Hogan & Hartson attorneys who have represented the Kanter family authored any part of this brief. Furthermore, no person or entity other than *amicus curiae* or Hogan & Hartson made a monetary contribution to the preparation and submission of this brief.

Inc., 519 U.S. 202 (1997) (merits stage); *Pierce* v. *Underwood*, 487 U.S. 552 (1988) (same); *Marshall* v. *Barlow's Inc.*, 436 U.S. 307 (1978) (same); *Deaton* v. *United States*, 124 S. Ct. 1874 (2004) (petition stage); *McNab* v. *United States*, 124 S. Ct. 1406 (2004) (same); *Gross* v. *Commissioner*, 537 U.S. 827 (2002) (same); *Walters* v. *Metropolitan Educ. Enters., Inc.*, 516 U.S. 1171 (1996) (same).

This brief is filed with the written consent of all parties pursuant to this Court's Rule 37.3(a); the requisite consent letters have been filed with the Clerk.

INTRODUCTION

The central issue in this case is whether the United States Tax Court's secretive handling of reports filed by its Special Trial Judges under Tax Court Rule 183 comports with the Due Process Clause of the Fifth Amendment.

Congress has authorized the Chief Judge of the Tax Court to "appoint Special Trial Judges who shall proceed under such rules and regulations as may be promulgated by the Tax Court." 26 U.S.C. § 7443A(a). Rule 183 provides that, following the conduct of a trial by an STJ, the STJ "shall submit a report, including findings of fact and opinion, to the Chief Judge," who will assign the case to a Judge or Division of the Tax Court. Tax Ct. R. 183(b). The rule also provides that the STJ's report—including the findings of fact therein—"shall be presumed to be correct," Tax Ct. R. 183(c), and given deference by the Judge or Division to which it is assigned. *See id.* ("Due regard shall be given to the circumstance that the [STJ] had the opportunity to evaluate the credibility of witnesses"); *see also Freytag* v. *Commissioner*, 501 U.S. 868, 874 n.3 (1991) (STJ's factual findings are reviewed by a Tax Court Judge under a "deferential standard"). Subject to those constraints, the Judge or Division to which the case is assigned may adopt, modify, or reject the STJ's report in whole or in part; receive additional evidence; order oral argument; or recommit the report with instructions. *See* Tax Ct. R. 183(c).

The practice of the Tax Court is to withhold the STJ's report from view. Neither the taxpayer nor a reviewing court of appeals ever sees the STJ's report, and that report is not made part of the record of the Tax Court's decision. And in those cases in which the Tax Court rejects the STJ's "presumed to be correct" findings, that fact goes undisclosed. Instead, the STJ prepares a revised report which the Tax Court adopts as its opinion—without ever revealing that the STJ's original findings were changed. As explained below, this secretive process is inconsistent with the Constitution's assurance of due process of law.

SUMMARY OF ARGUMENT

The Tax Court's failure to make the STJ's report available to a reviewing court of appeals violates the right to due process on appeal. The courts of appeals review decisions of the Tax Court for clear error, and the central feature of clear-error review is deference to the credibility judgments of the factfinder. Consistent with that approach, Tax Court Rule 183(c) provides that the STJ's findings of fact are "presumed to be correct" and that "[d]ue regard" shall be given to the STJ's determinations of witness credibility. The Tax Court's secretive process, however, impedes clear-error review by preventing the court of appeals from assessing whether the Tax Court gave proper deference to the STJ's factfinding and credibility determinations.

Due process also requires disclosure of the STJ's report on appeal because that document has legal effect. Under Rule 183, the STJ is required to prepare a report, and the Tax Court is required both to presume the correctness of the STJ's findings of fact and to give deference to the STJ's credibility determinations. The Rule 183 report thus has a legally-operative effect upon the Tax Court's ultimate decision. Underscoring this conclusion is *Freytag*, in which this Court held that STJs exercise significant governmental authority and rejected the Commissioner's contrary argument that STJs are mere "aides" of the Tax Court.

The three-part test of *Mathews* v. *Eldridge*, 424 U.S. 319 (1976), confirms that, as a matter of due process, STJ reports must be available to a reviewing court of appeals. First, the private interests at stake in a Tax Court case clearly are significant; in this case, for example, a taxpayer was found liable for civil tax fraud. Second, the Government has no readily apparent interest in denying to a reviewing court of appeals an STJ's report—which Tax Court rules already require STJs to prepare and submit to the Tax Court. Third, the Tax Court's refusal to release the STJ's report increases the risk of an erroneous deprivation of the taxpayer's property interest by impairing the court of appeals' ability properly to review the facts found by the Tax Court.

Transparency and openness in the adjudicatory process are essential to the actual and perceived fairness of the judicial system. Yet the Tax Court refuses to disclose the conclusions of its initial factfinders. In so doing, the Tax Court stands alone. Unlike STJ reports, the initial findings of magistrate judges, bankruptcy judges, and administrative law judges are part of the record on review.

The serious due process question raised by the Tax Court's secretive process can, however, be avoided by construing 26 U.S.C. §§ 7459(b) and 7461(a) to require disclosure of STJ reports. The former states that "all reports of the Tax Court" are "public records" while the latter requires the Tax Court to "report in writing all its findings of fact, opinions, and memorandum opinions." Pursuant to the doctrine of constitutional doubt, these statutes should be construed to mandate disclosure of the STJ's report, thus obviating the substantial issue of due process that would otherwise arise from the Tax Court's practice of withholding those reports from reviewing courts of appeals.

ARGUMENT

I. APPELLATE REVIEW OF TAX COURT DECISIONS WITHOUT ACCESS TO THE STJ'S REPORT VIOLATES DUE PROCESS.

The Due Process Clause of the Fifth Amendment guarantees that "[n]o person shall be * * * deprived of life, liberty, or property, without due process of law." U.S. Const., amend. V. "[T]he Due Process Clause, like its forbear in the Magna Carta, was intended to secure the individual from the arbitrary exercise of the powers of government." *Daniels* v. *Williams*, 474 U.S. 327, 331 (1986) (internal citation and quotation marks omitted). "By requiring the government to follow appropriate procedures when its agents decide to 'deprive any person of life, liberty, or property,' the Due Process Clause promotes fairness in such decisions." *Id.*

"Because exaction of a tax constitutes a deprivation of property," procedures for the adjudication of tax liability must "satisfy the commands of the Due Process Clause." *McKesson Corp.* v. *Division of Alcoholic Beverages & Tobacco*, 496 U.S. 18, 36 (1990). Accordingly, a federal taxpayer, whether an individual or a business, has a constitutional right to a fair process for resolving tax disputes with the Internal Revenue Service. *See id.* at 39 (government must afford taxpayers "a fair opportunity to challenge the accuracy and legal validity of their tax obligation"); *Turner* v. *Wade*, 254 U.S. 64, 67-68 (1920) (taxpayer entitled to adequate process for challenging "the validity of a tax and the amount thereof").

Like the procedures governing the conduct of a trial or other initial level of adjudication, "the procedures used in deciding appeals must comport with the demands" of the Due Process Clause. *Evitts* v. *Lucey*, 469 U.S. 387, 393 (1985). Although there may be no constitutional right to appeal the decisions of the Tax Court, because Congress determined that taxpayers should have a statutory right to do so, *see* 26 U.S.C. § 7482(a)(1), the Tax Court cannot utilize a process that forecloses meaningful appellate review consistent with

due process. And as explained below, the Tax Court's refusal to include the STJ's report in the record on appeal precludes fair and accurate appellate review.

A. Appellate Review For Clear Error Requires Access To The STJ's Report.

The twelve regional courts of appeals review decisions of the Tax Court "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury." 26 U.S.C. § 7482(a)(1); *see Freytag*, 501 U.S. at 891. Thus, courts of appeals review the Tax Court's factual findings for clear error. *Commissioner* v. *Duberstein*, 363 U.S. 278, 290-291 (1960); *see, e.g.*, *Andantech L.L.C.* v. *Commissioner*, 331 F.3d 972, 976 (D.C. Cir. 2003) (citing *Duberstein*); *Ballantyne* v. *Commissioner*, 341 F.3d 802, 807 (8th Cir. 2003) (same).[2]

The cornerstone of clear-error review is deference to the initial factfinder's opportunity to observe witnesses first-hand and to make credibility determinations. As this Court has explained, "[t]rial judges have the unique opportunity to consider the evidence in the living courtroom context, while appellate judges see only the cold paper record." *Gasperini* v. *Center for Humanities, Inc.*, 518 U.S. 415, 438 (1996) (internal citations and quotation marks omitted). "Face to face with living witnesses the original trier of fact holds a position of advantage" from which, in the case of the STJ, both the Tax Court Judge and appellate judges "are excluded." *United States* v. *Oregon State Med. Soc'y*, 343 U.S. 326, 339 (1952) (quotation marks and citation omitted); *see also Holiday* v. *Johnson*, 313 U.S. 342, 352 (1941) ("One of the essential elements of the determination of crucial facts is the weighing and appraising of testimony.").

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2 " 'A finding is "clearly erroneous" when although there is evidence to support it, the reviewing court on the entire evidence is left with the definite and firm conviction that a mistake has been committed.' " *Duberstein*, 363 U.S. at 291 (quoting *United States* v. *United States Gypsum Co.*, 333 U.S. 364, 395 (1948)).

When findings are based on determinations regarding the credibility of witnesses, the appellate court owes "even greater deference to the trial court's findings; for only the trial judge can be aware of the variations in demeanor and tone of voice that bear so heavily on the listener's understanding of and belief in what is said." *Anderson* v. *City of Bessemer City, N.C.*, 470 U.S. 564, 575 (1985) (citing *Wainwright* v. *Witt*, 469 U.S. 412 (1985)); *see also Webb* v. *Commissioner*, 394 F.2d 366, 380 (5th Cir. 1968) (noting the importance of observation of witness in Tax Court proceeding and deferring to the "benefit of live testimony where the demeanor of the witnesses would be gauged and evaluated").

This Court has stressed that determining "the weight and credibility of the evidence is the special province of the trier of fact." *Inwood Labs., Inc.* v. *Ives Labs., Inc.*, 456 U.S. 844, 856 (1982). Moreover, "[t]he rationale for deference to the original finder of fact is not limited to the superiority of the trial judge's position to make determinations of credibility. The trial judge's major role is the determination of fact, and with experience in fulfilling that role comes expertise." *Anderson*, 470 U.S. at 574-575.

In requiring that the STJ's factfinding shall be "presumed to be correct" and insisting upon "[d]ue regard" for the STJ's credibility determinations, Tax Court Rule 183(c) mirrors the standard for appellate review of findings of fact from district courts. Federal Rule of Civil Procedure 52(a) states that, in reviewing a trial judge's factual findings, "due regard shall be given to the opportunity of the trial court to judge the credibility of the witnesses" and provides that such findings shall be reviewed only for clear error. *See Inwood Labs.*, 456 U.S. at 855 (Rule 52(a) "recognizes and rests upon the unique opportunity afforded the trial court judge to evaluate the credibility of witnesses and to weigh the evidence.") (citing *Zenith Radio Corp.* v. *Hazeltine Research, Inc.*, 395 U.S. 100, 123 (1969)).[3]

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[3] The importance of seeing a witness in making a credibility determination is also reflected in Federal Rule of Civil Procedure

Disregarding this Court's cases and pronouncements on the importance of credibility determinations and the critical vantage point of the initial factfinder in making credibility determinations—as well as its own rule—the Tax Court refuses to permit appellate courts to review the STJ's report. In so doing, the Tax Court precludes a constitutionally proper appeal because the centerpiece of clear-error review is deference to the credibility determinations and findings of the judicial officer who actually observed the witnesses. Due to the Tax Court's secretive process, an appellate court is left to review a credibility finding with the same degree of deference whether that finding was made by the Tax Court based on a cold record or by the STJ who presided over the trial. The Tax Court's decision to keep the STJ report secret also prevents an appellate court from determining if the Tax Court followed its own rules. Due process requires the Tax Court to follow its self-imposed rules and to create a record adequate to confirm whether it has done so. *See Giacco* v. *State of Pennsylvania*, 382 U.S. 399, 403 (1966) ("Certainly one of the basic purposes of the Due Process Clause has always been to protect a person against having the Government impose burdens upon him except in accordance with the valid laws of the land."). Only when the record for appellate review includes the findings of the initial factfinder, instead of merely those findings as filtered through a Tax Court Judge, can appellate review be fair and meaningful.

The refusal of the Tax Court to permit appellate court access to the STJ report implicates due process in two ways. First, even though due process mandates that factfinding not take place by proxy, the Tax Court Judge (who has not heard the witnesses) may, as alleged in this case, overturn the STJ's findings and credibility judgments. The Tax Court's secret process does not permit the appellate court to evaluate that reversal. Second, the Tax Court Judge may simply accept the

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63, which provides that when a judge is no longer able to proceed with a hearing or trial that has commenced, the successor judge shall recall any witness whose testimony is material and disputed at the request of a party.

STJ's findings without undertaking the review required by Tax Court Rule 183(c). *Cf. Erhard* v. *Commissioner*, 46 F.3d 1470, 1476 (9th Cir.) ("Indeed, permitting the litigants to file objections to the special judge's report might well decrease the danger that the tax court will simply endorse the report without review.") (citation omitted), *cert. denied*, 516 U.S. 930 (1995). Either of these alternatives offends due process.

In order to review the Tax Court's factual findings for clear error, the appellate court must know the genesis of those factual findings. Although the Tax Court opinion states that it "agrees with and adopts the opinion of the Special Trial Judge" (App. to *Kanter* Pet. at 98a), and the STJ's *opinion* contains findings of fact, those findings may completely reverse the initial findings of fact that Tax Rule 183(b) requires to be contained in the STJ's *report*. And by keeping the original STJ report under wraps, neither the individual taxpayer nor the appellate court knows whether the crucial factual determinations on credibility and other issues contained in the Tax Court-adopted STJ opinion are the same or different from the factual findings in the STJ's report. If the findings are different, neither the taxpayer nor the appellate court knows if or how the Tax Court complied with the mandate of Tax Court Rule 183(c) to give "[d]ue regard" to the fact that the STJ "had the opportunity to evaluate the credibility of witnesses" and that the STJ's findings of fact in the report "shall be presumed to be correct." Tax Ct. R. 183(c). While the Tax Court opinion gives the impression that the STJ opinion is the STJ report,[4] there is simply no way to know whether, how, and why the Tax Court opinion modifies or reverses the factual findings in the STJ report

[4] In fact, both Courts of Appeals in the underlying cases specifically assumed that the STJ report and the STJ opinion were the same document. *See Ballard* v. *Commissioner*, 321 F.3d 1037, 1040 (11th Cir. 2003) ("Judge Dawson issued the opinion of the Tax Court in which the Tax Court both approved of and adopted Special Trial Judge Couvillion's *report*.") (emphasis added); *Estate of Kanter* v. *Commissioner*, 337 F.3d 833, 840-841 (7th Cir. 2003).

without access to the report itself. Appellate review on such terms is inadequate. *Cf. West Ohio Gas Co.* v. *Public Utils. Comm'n of Ohio*, 294 U.S. 63, 69 (1935).[5]

Because no Tax Court Judge is present at a trial before an STJ, the STJ is the exclusive finder of fact with respect to evaluating the credibility of witnesses. Rule 183(c) indicates that in the Tax Court, as in every other adjudicative forum, an initial factfinder's credibility assessments should not be second-guessed by those who were not present. *See Morgan* v. *United States*, 298 U.S. 468, 481 (1936) ("The one who decides must hear"). Live testimony provides the STJ access to nuances in a witness's physical reactions, demeanor, and tone of voice that cannot be gleaned from merely reading the transcript. In *Goldberg* v. *Kelly*, 397 U.S. 254 (1970), in which the Court evaluated a procedure that prevented welfare recipients from appearing personally before the official who actually determined eligibility, the Court said that "[p]articularly where credibility and veracity are at issue, * * * written submissions are a wholly unsatisfactory basis for decision." *Id.* at 269. Likewise, the cold record is a wholly unsatisfactory basis for the Tax Court's credibility determinations, and meaningful appellate review depends on knowing what was the basis for the credibility determination.

Additionally, this Court has recognized the importance of weighing the agreement (or lack thereof) between lower courts on factual findings. "That great weight is to be given to the findings of fact by the two lower courts is a rule of wisdom in the exercise of the reviewing power of this

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[5] The concern that the Tax Court Judge will fail to give the proper deference and presumption of correctness to the STJ's credibility determinations and factual findings is heightened by the fact that STJs lack the guarantees of judicial independence enjoyed by Article III judges. *See Freytag*, 501 U.S. at 912 (Scalia, J., concurring in part and concurring in the judgment) (STJs "lack life tenure; their salaries may still be diminished; they are still removable by the President"). As explained below, *see infra* at 13, this observation does not equate to a determination that STJs are mere "aides" or "staff" of the Tax Court.

Court." *Offutt* v. *United States*, 348 U.S. 11, 15 (1954); *see also Easley* v. *Cromartie*, 532 U.S. 234, 242 (2001) ("Where an intermediate court reviews, and affirms, a trial court's factual findings, this Court will not 'lightly overturn' the concurrent findings of the two lower courts.") (quoting *Neil* v. *Biggers*, 409 U.S. 188, 193 n.3 (1972)); *Corn Prods. Refining Co.* v. *Commissioner*, 350 U.S. 46, 51 (1955) ("[O]n essentially factual questions the findings of two courts should not ordinarily be disturbed.").

This same principle applies in the administrative context. *See Universal Camera Corp.* v. *NLRB*, 340 U.S. 474, 496 (1951) ("[E]vidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion."); *NLRB* v. *Stor-Rite Metal Prods., Inc.*, 856 F.2d 957, 964 (7th Cir. 1988) (noting that when the NLRB "rejects the findings of the ALJ, a special problem of administrative review arises[,]" and the reviewing court may view the evidence supporting the Board's conclusion as "less substantial than it would be if the Board and the ALJ had reached the same conclusion") (internal citations and quotation marks omitted); *Simon* v. *Simmons Foods, Inc.*, 49 F.3d 386, 389-390 (8th Cir. 1995) ("While much deference is usually accorded to an agency's expertise and discretion when the agency adopts the findings of the ALJ, a slightly different rule applies when the administrative agency rejects the ALJ's findings. An agency departing from the findings of the ALJ must show that it gave attentive consideration to the ALJ's conclusions.") (internal citations omitted).

At bottom, the Tax Court's secreting of the STJ's report offends due process because it is important for an appellate court, in determining the degree of deference to be given to the Tax Court's factual findings, to know whether and why the Tax Court agreed with or rejected the STJ's findings of fact and credibility determinations. If the Tax Court agreed with the STJ's conclusions, appellate review for clear error is

properly deferential. But if the Tax Court rejected the factfinding and credibility determinations of the STJ who actually saw and heard the witnesses, further scrutiny is required on appeal. The Tax Court's refusal to disclose the STJ's report thus impedes the proper exercise of appellate review in violation of the Due Process Clause.

B. The STJ's Report Must Be Disclosed On Appeal Because It Has Legal Effect.

The denial of the STJ's Rule 183 report to an appellate court that is reviewing a decision of the Tax Court cannot be squared with the requirements of due process for the further reason that that report is a document having legal effect.

Rule 183 makes it mandatory for the STJ to produce a report: the STJ "*shall* submit a report, including findings of fact and opinion." Tax Ct. R. 183(b) (emphasis added). The rule then directs that the STJ's findings of fact "shall be presumed to be correct" and that deference—"[d]ue regard"—shall be given to the STJ's evaluation of the credibility of witnesses. Tax Ct. R. 183(c); *see also Freytag*, 501 U.S. at 874 n.3 ("deferential standard" applies to Tax Court review of STJ's factfinding). The Rule 183 report thus is a document that has a legally-operative effect upon the ultimate decision of the Tax Court.

That the Rule 183 report is a document with legal effect is underscored by the fact that STJs are not mere "aides" or "staff" of the Tax Court. Indeed, the powers and duties of STJs place them in an entirely different category from law clerks or other judicial assistants.

In *Freytag*, this Court held that STJs are "inferior Officers" of the United States (U.S. Const. art. II, § 2, cl. 2) who exercise significant governmental authority. *See Freytag*, 501 U.S. at 881. The *Freytag* Court rejected the Commissioner's contrary argument that an STJ "acts only as an aide to the Tax Court judge responsible for deciding the case" and that STJs should be deemed mere employees of the court

"because they lack authority to enter a final decision." *Id.* at 880, 881.

In rejecting that argument, the *Freytag* Court said that the Commissioner had "ignore[d] the significance of the duties and discretion that special trial judges possess." *Id.* The Court observed that "[t]he office of special trial judge is 'established by Law,' Art. II, § 2, cl. 2," and that an STJ's "duties and functions are * * * delineated in a statute." 501 U.S. at 881. The Court also noted that STJs "perform more than mere ministerial tasks. They take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders. In the course of carrying out these important functions, the special trial judges exercise significant discretion." *Id.* at 881-882.

In short, it cannot be consistent with due process for the Tax Court to withhold from a reviewing court of appeals a document that is legally required under Tax Court rules; prepared by a judicial officer vested with significant governmental authority; and having a legal effect upon the Tax Court's decision in the case.

C. *Mathews* v. *Eldridge* Requires Disclosure Of The STJ's Report To An Appellate Court.

As this Court recently confirmed, the test set forth in *Mathews* v. *Eldridge*, *supra*, is "[t]he ordinary mechanism * * * for determining the procedures that are necessary to ensure that a citizen is not 'deprived of life, liberty, or property, without due process of law.' " *Hamdi* v. *Rumsfeld*, 124 S. Ct. 2633, 2646 (2004) (plurality opinion of O'Connor, J.) (quoting the Fifth Amendment); *see also Burns* v. *United States*, 501 U.S. 129, 148 (1991) (Souter, J., dissenting) ("The *Mathews* analysis has thus been used as a general approach for determining the procedures required by due process whenever erroneous governmental action would infringe an individual's protected interest") (citing cases applying *Mathews* in a wide variety of circumstances). The *Mathews* test is properly applied here to determine the

requirements of due process in the tax adjudication context. *See McKesson Corp.*, 496 U.S. at 36 n.17.

Under *Mathews*, three factors are judicially analyzed and balanced to ascertain whether a challenged governmental procedure comports with due process:

> First, the private interest that will be affected by the official action; second, the risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards; and finally, the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail. [424 U.S. at 335.]

Here, the application of the *Mathews* test leads to the conclusion that due process requires the disclosure of the STJ's report to a reviewing court of appeals.

The private interests at stake in Tax Court cases are undoubtedly significant. This Court has recognized that, like deprivations of liberty interests, the deprivation of a property interest can be severe. *See, e.g., FDIC* v. *Mallen*, 486 U.S. 230, 243 (1988). In this case, Burton Kanter was found liable for civil tax fraud—a judgment that carries enormous pecuniary and other consequences. And that is not just a temporary deprivation; it is a permanent one. *Cf. City of Los Angeles* v. *David*, 538 U.S. 715, 717 (2003) (per curiam).[6]

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[6] The Tax Court's secretive process also has a broader impact upon the Nation's small businesses and economic growth. Small businesses are crucial to the American economy and job creation. There are some 22.4 million small businesses in the United States, representing 99 percent of all employers and creating two-thirds to three-quarters of net new jobs. *See* House of Representatives, Small Business Comm., Small Business Facts, *available at* http://wwwc.house.gov/smbiz/smallBusinessFacts/smallBusinessFacts.asp. When a small business is subjected to erroneous taxation—*i.e.*, the imposition of taxes that the business is not, in fact, obligated to pay—it undermines the viability of the small business. Yet the Tax Court's secretive handling of STJ reports can only

The governmental interest in withholding the STJ's report from a reviewing court of appeals, conversely, is not readily apparent. Tax Court Rule 183 already requires STJs to prepare reports and file them with the Tax Court. The burden of including that document in the record on appeal is negligible. And it is hard to see what legitimate governmental interest could be served by denying the parties and the appellate court access to a document that has independent legal significance.

The remaining *Mathews* factor—the risk of an erroneous deprivation due to the Tax Court's refusal to release the STJ's report—points strongly in favor of releasing such reports on appeal. Appellate review of initial adjudications affecting significant private interests is a defining characteristic of the American legal system because such review is essential to reaching fair and accurate judgments. Accordingly, this Court has recognized the importance of appellate review to obtaining correct adjudications, in both civil and criminal contexts. *See Cooper Indus., Inc.* v. *Leatherman Tool Group, Inc.*, 532 U.S. 424, 436 n.9 (2001); *Griffin* v. *Illinois*, 351 U.S. 12, 18 (1956) (plurality opinion). And, as shown above, nondisclosure of the STJ's report impairs a court of appeals' ability to review the Tax Court's factfinding. By lifting the veil off these reports, this Court can only improve the accuracy of appellate decision making. *See Joint Anti-Fascist Refugee Comm.* v. *McGrath*, 341 U.S. 123, 171 (1951) (Frankfurter, J., concurring) ("Secrecy is not congenial to truth seeking").

The risk of erroneous deprivation is exemplified in this case by the fact that both of the courts below assumed that the STJ "opinion" adopted by the Tax Court was in fact the STJ's Rule 183 report without any evidence to support this assumption. *See Ballard*, 321 F.3d at 1040 ("Judge Dawson issued the opinion of the Tax Court in which the Tax Court both approved of and adopted Special Trial Judge Couvil-

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discourage small businesses from resorting to the Tax Court to contest erroneous taxation.

lion's *report*.") (emphasis added); *Estate of Kanter*, 337 F.3d at 840-841. An appellate court cannot conduct a meaningful review if it is not sure whether the STJ's report and opinion are one and the same.

D. The Tax Court Stands Alone In Its Secret Process.

Transparency is one of the hallmarks of a fair judicial process. As Justice Frankfurter stated in *McGrath*, 341 U.S. at 170, "fairness can rarely be obtained by secret, one-sided determination of facts decisive of rights." *Accord Connecticut* v. *Doehr*, 501 U.S. 1, 14 (1991). A transparent process is also necessary to ensure public confidence in the integrity of the judicial system. Thus, this Court has stressed that "[o]penness * * * enhances * * * the appearance of fairness so essential to public confidence in the system." *Press-Enterprise Co.* v. *Superior Court of Cal., Riverside County*, 464 U.S. 501, 508 (1984); *see also Richmond Newspapers, Inc.* v. *Virginia*, 448 U.S. 555, 572 (1980) ("People in an open society do not demand infallibility from their institutions, but it is difficult for them to accept what they are prohibited from observing.").

The secrecy with which the Tax Court treats the STJ reports undermines the confidence of both the public and the appellate courts that the Tax Court complied with its own rule requiring it to "presume[ ] to be correct" the STJ's findings of fact and to give "[d]ue regard" to the STJ's credibility determinations. Tax Ct. R. 183(c). Disclosure of the STJ report would lend transparency to the Tax Court's process and facilitate appellate review of that court's judgments. As it is, the Tax Court's current secretive procedures cast a shadow over the integrity of its factfinding. The lack of transparency in the Tax Court proceedings invariably and unnecessarily gives rise to speculation about how and why a case was decided as it was.

Not surprisingly, the Tax Court stands alone in refusing to ensure proper appellate review by secreting the reports of initial factfinders. The STJ "acts in a capacity not dissimilar to that of a magistrate in district court." *Estate of Smith* v.

Commissioner, 638 F.2d 665, 669 (3d Cir. 1981). But the reports of magistrate judges, and other similar judicial officers, including bankruptcy judges, special masters, and administrative law judges, must be part of the record on review. *See* 28 U.S.C. § 636(b)(1)(C) ("the magistrate judge shall file his proposed findings and recommendations * * * with the court and a copy shall forthwith be mailed to the parties"); Fed. R. Bankr. P. 9033(a) ("the bankruptcy judge shall file proposed findings of fact and conclusions of law"); Fed. R. Civ. P. 53(e) ("master who makes an order must file the order and promptly serve a copy on each party"); Fed. R. Civ. P. 53(f) (requiring special master to file report and promptly serve on the parties "unless the court directs otherwise"); 5 U.S.C. § 557(c) ("All [preliminary agency] decisions, including initial, recommended, and tentative decisions, are a part of the record * * *."). This Court also provides parties access to the reports of its special masters, to which the parties may make exceptions. *See, e.g.*, *Kansas* v. *Colorado*, 533 U.S. 1, 5-6 (2001); *Colorado* v. *New Mexico*, 467 U.S. 310, 313 (1984).

As the courts of appeals have repeatedly recognized, transparency serves a critical role in the appellate review process. For instance, if the appellate court does not have access to the factual findings of the magistrate judge, it cannot ensure that the district court appropriately performed its review nor can it correctly perform its own clear-error review. *See, e.g.*, *Cooper-Houston* v. *Southern Ry.*, 37 F.3d 603, 604 (11th Cir. 1994) (overruling summary judgment on the ground that the district court was "bound to defer to the factual determinations of the magistrate judge unless those findings were clearly erroneous"); *Shabazz* v. *Askins*, 980 F.2d 1333, 1334-35 (10th Cir. 1992) (finding that the district court abused its discretion in adopting a magistrate's report that incorrectly weighed disputed facts); *Phinney* v. *Wentworth Douglas Hosp.*, 199 F.3d 1, 4 (1st Cir. 1999) (determining that the magistrate's account of the facts was not clearly erroneous and therefore affirming the district court's judgment).

The same need for access to the initial factfinder's report holds true in the review of decisions of bankruptcy judges and administrative law judges. *See, e.g., In re Webb*, 954 F.2d 1102, 1108 (5th Cir. 1992) ("The district court did not properly apply the clearly erroneous standard of review to the findings of the bankruptcy court. Had it done so, it would have concluded, as [d]o we, that the bankruptcy court's findings were plausible, and, therefore, were not clearly erroneous."); *Ewing* v. *NLRB*, 732 F.2d 1117, 1118 (2d Cir. 1984) (overruling decision of NLRB to reverse ALJ's credibility determinations because "[i]t is the task of trial judges to separate factual wheat from evidentiary chaff, and appellate courts must accord great deference to these determinations[,] [and] [t]he same policies apply in the administrative context when decisions of the finder of fact are brought under review").

A constitutionally proper appeal requires an appellate court to be able to review the findings of the STJ—the judicial officer who presided over the trial, observed the witnesses, and made the critical credibility determinations. The Tax Court's refusal to provide a complete record for appellate review and insistence on judicial secrecy violates due process. This Court should condemn that practice—a practice that does not comport with the fair and open process that litigants and the public expect of our judicial institutions.

II. INTERPRETING 26 U.S.C. §§ 7459 AND 7461 TO REQUIRE DISCLOSURE OF THE STJ'S REPORT AVOIDS THE DUE PROCESS ISSUE.

Under this Court's doctrine of constitutional doubt, "where an otherwise acceptable construction of a statute would raise serious constitutional problems, the Court will construe the statute to avoid such problems unless such construction is plainly contrary to the intent of Congress." *Edward J. DeBartolo Corp.* v. *Florida Gulf Coast Bldg. & Constr. Trades Council*, 485 U.S. 568, 575 (1988); *see also Ashwander* v. *TVA*, 297 U.S. 288, 348 (1936) (Brandeis, J., concurring); *United States ex rel. Attorney General* v. *Delaware & Hudson Co.*, 213 U.S. 366, 408 (1909) ("[W]here a statute is

susceptible of two constructions, by one of which grave and doubtful constitutional questions arise and by the other of which such questions are avoided, our duty is to adopt the latter.").

As shown above, the Tax Court's failure to disclose STJ reports raises a serious due process question. That question can be avoided, however, by interpreting two provisions of the Internal Revenue Code—26 U.S.C. §§ 7459(b) and 7461(a)—to require disclosure of such reports. Section 7461(a) provides that "all reports of the Tax Court * * * shall be public records open to the inspection of the public." And Section 7459(b) states that "[t]he Tax Court shall report in writing all its findings of fact, opinions, and memorandum opinions." These statutes can and should be construed to require disclosure of the STJ's report and thereby avoid the substantial due process issue that would otherwise arise. *Cf. Burns*, 501 U.S. at 138 (avoiding due process problem by construing Fed. R. Crim. P. 32 to prohibit district court from departing upward from Sentencing Guidelines range without providing notice of its intent to do so).

The plain language of both Section 7461(a) and 7459(b) would seem to encompass the STJ reports required by Rule 183 and the contents of those reports. Section 7461(a) makes publicly available all "reports" of the Tax Court. A Rule 183 report clearly is a "report"; indeed, that is the very term used in Rule 183. Section 7459(b), meanwhile, applies to all "findings of fact" and "opinions," and the STJ's report is expressly required to "includ[e] findings of fact and opinion." Tax Ct. R. 183(b). Thus, STJ reports appear to fall squarely within the coverage of these statutes. At the very least, it cannot be said that it would be "plainly contrary to the intent of Congress," *Edward J. DeBartolo Corp.*, 485 U.S. at 575, to construe these statutes so as to avoid the due process problem entailed by withholding STJ reports from a reviewing court of appeals.

CONCLUSION

For the foregoing reasons, the judgments below should be reversed.

Respectfully submitted,

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IN THE

Supreme Court of the United States

CLAUDE M. BALLARD, ET UX.,
ESTATE OF BURTON W. KANTER, ET AL.,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURTS OF APPEALS FOR THE SEVENTH AND ELEVENTH CIRCUITS

BRIEF OF *AMICI CURIAE* SENATOR DAVID PRYOR; THE ESTATE OF ROBERT W. LISLE; AND THE ESTATE OF DONNA M. LISLE IN SUPPORT OF PETITIONERS

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QUESTION PRESENTED

Whether the Due Process clause of the Fifth Amendment obliges the Tax Court to disclose the findings of the Special Trial Judge, when the Tax Court's rules oblige the trial judge to make such findings and require the Tax Court to presume that these findings are correct.

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I. WHEN AN OFFICER'S FINDINGS ARE PRESUMED TO BE CORRECT AS A MATTER OF LAW, THEN THEY MUST BE DISCLOSED TO PARTIES, BECAUSE THEY PLAY A DECISIVE ROLE IN DEFINING THE SUFFICIENCY OF THE PARTIES' EVIDENCE. 5

A. Because the STJ's report is entitled to a presumption of being correct under Rule 183(c), this report is critically important for assessing the sufficiency of the evidence supporting the Tax Court's opinion. 6

B. The Tax Court must disclose the STJ's report as part of its general duty to disclose findings that critically affect the sufficiency of the evidence underlying the Tax Court's decision. 9

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D. Because the STJ's report is legally entitled to a presumption of being correct under Rule 183(c), that report is distinguishable from the reports of the Division of the Tax Court. 20

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INTERESTS OF *AMICI CURIAE*[1]

Hon. David Pryor served as United States Senator from Arkansas from 1979 to 1996 and as a United States Representative from 1966 to 1973. While in the Senate, Senator Pryor served on the Senate Finance Committee, chairing a subcommittee with responsibility for oversight of the Internal Revenue Service. While in this position, he developed and introduced the first Taxpayer Bill of Rights which was enacted in 1988. *See* Omnibus Taxpayer Bill of Rights, Pub. L. No. 100-647, §§6226-35, 102 Stat. 3342, 3731. As a Member of the House of Representatives, Senator Pryor supported and voted for the Tax Reform Act of 1969, §951, Pub. L. No. 91-172, 83 Stat. 730, which, in order to ensure neutrality and procedural regularity, removed the Tax Court (previously the Board of Tax Appeals) from the Executive Branch and transformed it into an Article I Court. *See* 115 Cong. Rec. H22809, 91st Cong. 2d Sess. (Aug 7, 1969) (roll call vote).

Senator Pryor's actions have been motivated by an abiding belief that taxpayers in the United States have basic rights, including the right to due process of law, a right that is infringed by the proceedings to which the taxpayers here have been subjected. In speaking on the floor of the Senate in support of his landmark 1988 legislation he said "The passage of the taxpayers' bill of rights will send, I think, a very clear message to our country and to all taxpayers, small and large, that taxpayers do in fact have certain basic due process rights ...." 134 Cong. Rec. S15073, S15074, 100th

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[1] In compliance with Supreme Court Rule 37.6, *amici* state that no counsel for a party authored this brief in whole or in part. No person other than *amici* or their counsel made a monetary contribution to the preparation or submission of this brief. Pursuant to Supreme Court Rule 37.3, copies of letters of consent to the filing of this brief have been lodged with the Court.

Cong. 2d Sess. (Oct. 7, 1988) (statement of Sen. Pryor). "Like any good citizen," he said, "I believe that everyone should pay his or her lawful share of taxes. That is the price of freedom. However, at the same time that we are allowing the IRS to be more intrusive into the lives of our citizens for the sake of compliance, we must also ensure that we maintain basic due process rights, which have eroded slowly but surely over these past two and one-half decades." 134 Cong. Rec. S4134, 100th Cong. 2d Sess. (April 15, 1988) (statement of Sen. Pryor). Senator Pryor seeks to put his views before this Court because of his conclusion that, despite his legislative efforts, the secret procedures now used by the Tax Court and at issue here deprive taxpayers of those basic rights.

Taxpayers Robert and Donna Lisle ("the Lisles") were parties in the Tax Court proceeding under review here. As provided for by 26 U.S.C. §7482(b)(1)(A), because of their legal residence the Lisles' appeal from the adverse decision of the Tax Court was heard by a different Court of Appeals, the United States Court of Appeals for the Fifth Circuit, in a different case than that under review by this Court. *See Estate of Lisle v. Commissioner*, 341 F.3d 364 (5th Cir. 2003). In that case, even despite the unavailability of the Special Trial Judges' report in this case, the Court of Appeals concluded that the credibility and other judgments of the Tax Court were insufficiently supported by the evidence to sustain the finding of fraud against Robert Lisle that formed the basis for most of the tax deficiency and penalties assessed against the Lisles. The Lisles died during the pendency of their appeal. Their estates appear before this Court as *amici curiae* because of the denial of due process that it is now clear was wrought by the routine practice of the Tax Court utilized in the proceeding in which the remaining deficiency against the Lisles — the amount of which remains to be determined on remand in their case — was assessed.

INTRODUCTION AND SUMMARY OF ARGUMENT

The issue in this case hinges on a principle of procedural transparency so basic that, outside of the Tax Court, it is universally observed by both courts and administrative agencies. This principle is that, if an agency or tribunal relies on a trial judge to hear testimony and, based on that hearing, to make factual findings that enjoy a presumption of being correct, then that agency or tribunal must disclose that judge's recommended findings to the parties whose rights are affected by them. The Tax Court has given special importance to the factual recommendations of the Special Trial Judge ("STJ") by providing in Tax Court Rule 183(c) that "the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Given that the Tax Court has invested the STJ's factual recommendations with a presumption of validity, the Tax Court must disclose those factual recommendations to the parties, because such presumptively valid findings help determine whether there is sufficient evidence underlying the Tax Court's decisions. Thus, the STJ's report has at least the same importance as a potentially decisive piece of evidence. Just as the Tax Court is obliged to disclose evidence on which its decisions rest, so too, the Tax Court is obliged to disclose recommended fact findings that it must presume to be correct.

Because the Tax Court has chosen to invest the factual recommendations contained in the STJ's report with a presumption of validity, those recommended findings cannot be regarded as the purely internal deliberations of the Tax Court. Internal deliberations (*e.g.*, law clerks' memos, staff attorney's recommendations, judge's draft opinions) need not be disclosed, because such deliberations are not legally relevant to the parties' proof or rights and do not limit the tribunal's discretion. The tribunal is, by contrast, not free to ignore completely the STJ's report, because the Tax

Court's own Rule 183(c) requires that this report be accorded a presumption of being correct. By conferring this legal force on the report, the Tax Court has taken it outside the realm of purely internal advice and transformed it into a potentially decisive aspect of the proof.

Disclosure of the STJ's report, therefore, is critically important if the parties are to know whether and to what extent the legal presumptions created by the STJ's report favors or undermines their case. Against this private interest in disclosure, the Tax Court has no legitimate interest in withholding this document from the parties. The Tax Court's Rule 183(b) already requires the STJ to submit such a report to the Tax Court. Therefore, disclosure imposes no additional paperwork or other fiscal or administrative burden on any governmental agency.

The only burden created by disclosure is the burden of transparency. By revealing the presumptively correct statement of facts to the parties and appellate courts, disclosure makes it possible for both to enforce the Tax Court's own rules. But no agency has a legitimate interest in evading appellate review. The Tax Court undoubtedly has broad discretion to structure the mechanisms by which the parties' testimony can be considered. The Tax Court has exercised this discretion by creating a system of hearings before STJs, in which the STJ's findings are presumed correct and "[d]ue regard shall be given to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses." Having chosen such a system for protecting the parties' right to present in-person testimony, the Tax Court cannot then undermine its own rules through a policy of bureaucratic secrecy.

ARGUMENT

THE DUE PROCESS CLAUSE OF THE FIFTH AMENDMENT OBLIGES THE TAX COURT TO DISCLOSE THE SPECIAL TAX JUDGE'S REPORT TO THE PETITIONERS, BECAUSE THESE FINDINGS, BEING PRESUMPTIVELY CORRECT AS A MATTER OF THE TAX COURT'S OWN RULES, CRITICALLY AFFECT THE SUFFICIENCY OF THE PARTIES' EVIDENCE AND BECAUSE THE TAX COURT FACES NO ADMINISTRATIVE BURDEN IN PROVIDING THE REPORT TO PETITIONERS.

This Court determines the specific requirements of procedural due process by weighing "the private interest that will be affected by the official action" against "the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail." *Mathews v. Eldridge*, 424 U.S. 319, 335 (1976). No hard and fast rule defines what sorts of procedures are constitutionally required. Instead, this Court performs a context-specific inquiry to determine whether the probable value of additional procedures in preventing an erroneous deprivation of some private interest outweighs the administrative burdens entailed by the procedure. *Id.* In making this *ad hoc* assessment, the Court takes guidance from customary administrative and judicial practices. *Honda Motor Co., Ltd. v. Oberg*, 512 U.S. 415, 430 (1995) (citing decisions for the proposition that "traditional practice provides a touchstone for constitutional analysis" in due process cases). Procedures long in use by a wide array of governmental decision-makers have so withstood the test of time that they cannot be regarded as unduly burdensome. *Murray's Lessee v. Hoboken Land & Improvement Co.*, 18 How. 272, 277 (1856) (in defining what due process requires, "we must look to those settled usages and modes of proceeding existing in the

common and statute law of England, before the emigration of our ancestors, *and which are shown not to have been unsuited to their civil and political condition by having been acted on by them* after the settlement of this country") (emphasis added)

Judged by this standard, there can be little doubt that the Fifth Amendment's due process clause requires disclosure of the adjudicative fact-findings of trial judges, administrative law judges, and other initial factfinders *whenever the law invests those findings with the presumption of being correct.* Such disclosure is certainly sanctified by tradition: it has always been virtually the universal practice even in administrative tribunals as well as Article I courts.[2] Two reasons jus-

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[2] Under section 557 of the Administrative Procedure Act, the reports of hearings officers automatically become part of the administrative record. 5 U.S.C. §557(c). Federal law also requires Article I judges such as federal magistrates and bankruptcy judges to disclose their findings to the parties. 28 U.S.C. §636(b)(1)(C) ("The magistrate judge shall file his proposed findings and recommendations under subparagraph (B) with the court and a copy shall forthwith be mailed to all parties"); Bankr. R. 9033(a) (In non-core proceedings, "[t]he clerk shall serve forthwith copies [of bankruptcy judge's findings of fact] on all parties by mail and note the date of mailing on the docket"); Bankr. R. 9022 (notice and service of bankruptcy judges' orders and judgments). To counsel's knowledge, the Tax Court's policy of withholding the reports of special trial judges is unique among federal and state agencies and courts. As Judge Cudahy noted in his dissenting opinion, "[e]ven the Commissioner, at oral argument, acknowledged that in every milieu except that of the Tax Court, the document containing the findings or recommendations of the official conducting the trial are available to a court reviewing the operative decision." *Estate of Kanter v. Comm'r,* 337 F.3d 833, 874 (7th Cir. 2003).

The Commissioner maintains that the procedures used by the Tax Court do not violate traditional procedural protections, because tax disputes are not governed by the customs governing common-law courts and because "Tax Court judges need not operate in a manner precisely identical to Article III courts." Brief in Opposition to Certiorari at 17. These statements, however, attack straw men: neither *amici* nor Petitioners argue that the Tax Court is governed by the common law or by Article III. The question is whether the Tax Court complies with the procedural traditions of

tify a virtually universal practice of disclosure. First, when such fact-findings are invested by the law with a presumption of being correct, then they play a decisive role in determining whether the evidence before the final decision-maker is legally sufficient. Due process forbids keeping a party in the dark about such an essential aspect of the evidence. Second, where statute or regulation already requires an officer to provide written findings, the agency or court that relies on such findings faces no administrative burden whatsoever in disclosing them to the parties governed by them. In short, the cost to the government of disclosure is nil, while the effect of non-disclosure on the parties' capacity to present their proof is extraordinary. Thus, as explained in more detail below, common sense bolsters tradition in requiring disclosure of such findings.

I. WHEN AN OFFICER'S FINDINGS ARE PRESUMED TO BE CORRECT AS A MATTER OF LAW, THEN THEY MUST BE DISCLOSED TO PARTIES, BECAUSE THEY PLAY A DECISIVE ROLE IN DEFINING THE SUFFICIENCY OF THE PARTIES' EVIDENCE.

That disclosure of the STJ's report has enormous practical importance as a procedural safeguard rests on two well-settled principles. First, the STJ's report has at least the same weight as a potentially decisive piece of evidence, because the Tax Court's regulations invest this report with a presumption of being a correct statement of the facts. Tax Ct. R. 183(c). Second, the Tax Court has a duty to disclose to the Petitioners

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any tribunal, administrative or judicial, Article I or Article III. The answer is obvious: as Judge Cudahy noted, the Tax Court's refusal to disclose the factual recommendations of the STJ is simply unprecedented among any sort of tribunal and wholly at odds even with ordinary administrative practices. *Estate of Kanter*, 337 F.3d at 879 (Cudahy, J., dissenting).

all documents that have such critical bearing on whether there is sufficient evidence underlying the Tax Court's opinion. The inescapable corollary of these two propositions is that the Tax Court must disclose the contents of the STJ's report, because this report determines the sufficiency of the evidence in this case.

A. Because the STJ's report is entitled to a presumption of being correct under Rule 183(c), this report is critically important for assessing the sufficiency of the evidence supporting the Tax Court's opinion.

When statute or rule commands that a judge's initial fact-findings are presumptively correct, then those findings critically affect the sufficiency of the evidence underlying the final decision-maker's conclusion. This is true even when such findings are recommendations that the final decision-maker is entitled to overturn. As this Court has stated in *Universal Camera*, "evidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion." *Universal Camera Corp. v. NLRB*, 340 U.S. 474, 496 (1951). For this reason, the recommended findings of the trial judge are essential for a complete evaluation of the sufficiency of the evidence before a tribunal like the Tax Court, and such a tribunal must carefully consider such findings even if it ultimately decides to reject them. In *Universal Camera*'s categorical command, "[t]he findings of the examiner *are to*

be considered along with the consistency and inherent probability of testimony." *Id.* (emphasis added).[3]

The judge's initial factual recommendations are especially important when the judge is the only officer who has heard the witnesses' testimony first-hand. In cases where the credibility of the witnesses bears on the decision, the judge's recommended findings provide the ultimate decision-maker with the only mechanism through which to consider such credibility. *United States v. Raddatz*, 447 U.S. 667, 681 n.7 (1980) ("we assume it is unlikely that a district judge would *reject* a magistrate's proposed findings on credibility when those findings are dispositive and substitute the judge's own appraisal; to do so without seeing and hearing the witness or witnesses whose credibility is in question could well give rise to serious questions which we do not reach"); *Goldberg v. Kelly*, 397 U.S. 254, 269 (1970) ("Particularly where credibility and

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[3] Although *Universal Camera* addresses the standard for evaluating whether substantial evidence exists in the record to support an administrative agency's decision, its reasoning applies with equal force to review of the Tax Court's decisions for clear error. As this Court has noted, there are only subtle distinctions between the "clear error" standard and the "substantial evidence" standard. *Dickinson v. Zurko*, 527 U.S. 150, 162-163 (1999). Moreover, *Universal Camera* was rooted in the requirement contained in the Taft-Hartley Act, 61 Stat. 148, 29 U.S.C. §160(e) that the substantiality of the evidence be assessed in light of the "record considered as a whole." *Universal Camera*, 340 U.S. at 493. Likewise, in reviewing a court's fact-finding for "clear error," the reviewing court must consider the "entire evidence" and not merely those portions of the record that favor the trial court's factual conclusions. *Anderson v. City of Bessemer City*, 470 U.S. 564, 573 (1985) (quoting *United States v. United States Gypsum Co.*, 333 U.S. 364, 395 (1948)) ("'[a] finding is 'clearly erroneous' when *although there is evidence to support it*, the reviewing court on the *entire evidence* is left with the definite and firm conviction that a mistake has been committed'") (emphasis added). It follows that consideration of the STJ's report is just as essential for determining "clear error" in light of the "entire evidence" as consideration of a hearing officer's findings is for assessing whether "substantial evidence" in the "whole record" underlies an agency's decision.

ity and veracity are at issue ... written submissions are a wholly unsatisfactory basis for decision"). Thus, where credibility is at stake, the reports of the judge who observed such testimony will constitute an especially important part of the record, and *Universal Camera*'s principle that the administrative decision-maker must consider such reports applies with special force. Applying this principle to agency decisions, lower courts are unanimous in holding that the hearing officer's determinations of witnesses' credibility are part of the evidence that must be considered in order to determine whether an agency's decision is supported by substantial evidence.[4] It follows with at

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[4] *Chen v. GAO*, 821 F.2d 732, 734 (D.C. Cir. 1987) ("the evidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's than when he has reached the same conclusion" and agency reversals of the examiner "are normally scrutinized very carefully to ensure there is some reasoned explanation of the board's disagreement with the decision of the hearing officer"); *Parker v. Bowen*, 788 F.2d 1512, 1520 (11th Cir. 1986) ("We hold that the Appeals Council is not bound by the ALJ's credibility findings, but when it rejects such findings, it should ordinarily do so expressly, articulating the reasons for its conclusion"); *SKS Die Casting & Machining v. NLRB*, 941 F.2d 984, 988-89 (9th Cir. 1991)("The ALJ's contrary findings are one factor that we consider in evaluating whether the Board's findings are supported by substantial evidence"); *Citizens St. Bank v. Federal Deposit Ins. Corp.*, 718 F.2d 1440, 1445 (8th Cir.1983) ("The Board's departure from the ALJ's findings is vulnerable if it fails to reflect attentive consideration to the ALJ's decision"); *Chicago Tribune v. NLRB*, 974 F.2d 973, 935 (7th Cir. 1992) ("an administrative law judge's determinations of credibility are entitled to a certain weight by a reviewing court, because he sees and hears the witnesses and the Board has only a transcript of their testimony"); *Brock v. L.E. Myers Co., High Voltage Div.*, 818 F.2d 1270 (6th Cir. 1987) (requiring Occupational Safety and Health Review Commission to articulate reasons for failing to credit findings of an ALJ who had a unique opportunity to observe demeanor of witnesses); *Centre Property Management v. NLRB*, 807 F.2d 1264 (5th Cir. 1987) (applying "more searching" scrutiny to board's findings where they conflict with ALJs); *Blackburn v. Martin*, 982 F.2d 125, 128 (4th

least equal force that, when reviewing the entire evidence to determine whether the Tax Court committed "clear error" in its findings of fact, the STJ's assessment of credibility must be considered.

B. The Tax Court must disclose the STJ's report as part of its general duty to disclose findings that critically affect the sufficiency of the evidence underlying the Tax Court's decision.

Given the authority that Rule 183(c) confers on the STJ's report, this report must be disclosed to the Petitioners, because this report critically affects whether sufficient evidence underlies the Tax Court's opinion. The Tax Court is obliged by its own rules to take the STJ's report into consideration, because, according to Rule 183(c), this report must be presumed to be correct. It is a "relatively immutable [principle] in our jurisprudence" that "the evidence used to prove the Government's case must be disclosed to the individual so that he has an opportunity to show that it is untrue." *Greene v. McElroy*, 360 U.S. 474, 496-497

Cir. 1992) ("In conducting our review, we consider the entire record before us, including the ALJ's recommendation and any evidence that is contrary to the Secretary's determination"); *Eastern Engineering & Elevator Co v. NLRB*, 637 F.2d 191, 197 (3rd Cir. 1980) (NLRB's factual findings are overturned where NLRB "failed to accord due weight to the ALJ's findings of fact," because NLRB "was required to extend some, but not absolute, deference to the ALJ's determinations" on credibility of witnesses); *NLRB v. Cooper Union for Advancement of Science and Art*, 783 F.2d 29, 31 n.2 (2d Cir. 1986) ("We recognize that when the Board makes findings inconsistent with the ALJ, as here, the findings are more open to question than if the Board and the ALJ had reached the same result, but only if the evidence turns on the credibility of the witnesses"); *C.E.K. Indus. Mechanical Contractors, Inc. v. NLRB*, 921 F.2d 350, 355 (1st Cir. 1990) ("In cases such as this one, however, where the Board has reached a conclusion opposite of that of the ALJ, our review is slightly less deferential than it would be otherwise").

(1959). *See also Carter v. Kubler*, 320 U.S. 243, 247 (1943) ("The basic elements of such a [fair and full] hearing include the right of each party to be apprised of all the evidence upon which a factual adjudication rests, plus the right to examine, explain or rebut all such evidence"). It follows *a fortiori* that the STJ's report must also be disclosed, given the legal force with which the Tax Court has invested the STJ's report through Rule 183(c), because the findings of the STJ's report will affect the sufficiency of the evidence supporting the Tax Court's opinion. If the STJ's report is inconsistent with the Tax Court's view of the facts, then this inconsistency will weaken the evidentiary underpinning of the Tax Court's opinion and, where the evidence is otherwise close, suggest that the Tax Court committed clear error. Thus, the Tax Court can no more conceal the STJ's report from the Petitioners than it can conceal evidence that would affect judicial assessment of the evidentiary basis for the Tax Court's decision.

The importance of the STJ's report is especially great in this case because of the centrality of credibility evaluations to the Tax Court's finding of fraud. The Tax Court found that there was clear and convincing evidence that Burton Kanter was motivated by fraudulent intent in his alleged underpayment of taxes. Without disclosing what the STJ's report found concerning Kanter's testimony, the Tax Court's opinion relied, in part, on "the lack of credibility of Kanter's testimony." *Estate of Kanter v. Comm'r of Internal Revenue*, 337 F.3d 833, 846 (7th Cir. 2003). But this finding would be critically weakened if the STJ's report found that Kanter's testimony on his intentions was credible. Likewise, the Tax Court found that Ballard had committed tax fraud in part based on "Ballard's false and misleading testimony to the Tax Court." *Ballard v. Comm'r*, 321 F.3d 1037, 1043 (11th Cir. 2003). However, Ballard did not present testimony to "the Tax Court" but rather to the STJ. If the

STJ's report, presumed correct under Rule 183(c), had found that Ballard's testimony was neither false nor misleading, then this finding would severely undermine the evidentiary basis for the Tax Court's finding." In the words of *Universal Camera*, the evidence of fraud would become "less substantial" because "an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the [Tax Court's]." *Universal Camera*, 340 U.S. at 496. That the finding of fraudulent intent hinged on the undisclosed contents of that report is indicated by both the Seventh Circuit's and the Eleventh Circuit's opinions below, both of which upheld the Tax Court's finding of clear and convincing evidence of fraudulent intent in reliance on the Tax Court's assurance that the Tax Court's finding was consistent with the STJ's report. *Estate of Kanter*, 337 F.3d at 847. *Ballard v. Comm'r*, 321 F.3d at 1042 (relying on "critical fact" that the record as presented to us clearly reveals that the report adopted by the Tax Court is Special Trial Judge Couvillion's report").

Therefore, it was essential for Petitioners to know exactly what the STJ's report found concerning Kanter's and Ballard's intent in order to focus effectively their argument before the Tax Court and the Seventh and Eleventh Circuits. Under the Tax Court's rules, the Petitioners were permitted to file a post-trial motion for reconsideration of findings. Tax Ct. R. 161. But absent disclosure of the STJ's report, it was impossible for the Petitioners to discover and invoke any inconsistency between the STJ's report and the Tax Court's opinion as a basis for such a motion. In effect, by concealing the contents of the STJ's report, the Tax Court concealed from the Petitioners potentially decisive evidence that the Tax Court was legally obliged to consider as part of its decision-making process.

This Court has held that it is "illogical" for an administrative agency to deny a party the opportunity to

show that the expert opinions on which the agency relies are contradicted by other evidence. *Reilly v. Pinkus*, 338 U.S. 269, 275-76 (1949) ("It certainly is illogical, if not actually unfair, to permit witnesses to give expert opinions based on book knowledge, and then deprive the party challenging such evidence of all opportunity to interrogate them about divergent opinions expressed in other reputable books"). It is even more irrational for an Article I court to bar a party from having an opportunity to contradict the Tax Court's findings with the STJ's report. Unlike the medical dictionaries excluded from the evidence in *Reilly*, the STJ's report is not merely just one more piece of evidence. Rather, it is the legally authoritative statement of findings by the only judge to hear the testimony in this case, findings that the Tax Court was obliged by its own rules to presume correct and, at the very least, to consider carefully before rejecting them. Excluding such a report from the record even though the Tax Court was legally obliged to consider the report is tantamount to barring potentially decisive evidence from the record even though the court actually considered such evidence in reaching its decision.

In response to these concerns, the Tax Court assures the Petitioners and this Court that its own opinion gave appropriate regard to the STJ's report.[5] But this assertion confuses substance with procedure. The issue before this Court is not the substantive one of whether the Tax Court's opinion was supported by sufficient evidence and, therefore, should be affirmed on the merits. Rather the issue is the procedural

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[5] As proof of this assertion, the Tax Court notes that the STJ signed a declaration endorsing the Tax Court's opinion. Such a declaration, of course, shows only that the STJ endorsed the Tax Court's opinion, not that the STJ's report provided support for that opinion. Rule 183(c) invests only the latter with a presumption of being correct. That the STJ might have changed his mind after consulting with the Tax Court judges is, from an evidentiary point of view, irrelevant.

question of whether the Petitioners and the reviewing court of appeals received a fair opportunity to make an independent evaluation of the sufficiency of the evidence underlying the Tax Court's opinion. The Due Process clause requires that the Petitioners be given "the evidence used to prove the Government's case" so that the Petitioners "have an opportunity to show that it is untrue." *Greene v. McElroy*, 360 U.S. 474, 496-497 (1959). It is, of course, possible that the STJ's report supports the Tax Court's opinion in every respect. (If so, it is curious that the Tax Court refuses to release this report to Petitioners and the appellate courts). Regardless, this is a possibility that the Petitioners, the Seventh Circuit, the Eleventh Circuit, and, indeed, this Court are incapable of evaluating until the STJ's report is disclosed. *See Hoffman-LaRoche v. Kleindienst*, 464 F.2d 1068, 1072 (3rd Cir. 1972) (Requiring disclosure of advisory committee's report on which FDA's decision was based and noting that "[w]e cannot tell whether the failure to produce the Advisory Committee's report and its supporting documents was or was not prejudicial to Hoffmann until we examine them").

The Tax Court can no more support its decision by asserting that it had properly deferred to the undisclosed STJ's report than it could support its decision by referring to undisclosed testimony that allegedly supported the decision. *See Ohio Bell Tel. Co. v. PUC*, 301 U.S. 292, 303-04 (1937)(Deprivation of due process where Commission altered valuation of property relying on the "the strength of information secretly collected and never yet disclosed," because appellate court could not "intelligently decide that the findings of the Commission were supported by the evidence when the evidence that it approved was unknown and unknowable"). The Petitioners, like any other private party, is entitled to see the evidence for themselves and not rely on the Tax Court's *ipse dixit* that the STJ's report somehow supports — or does not under-

mine — the Tax Court's conclusions. As Justice Holmes observed ninety-one years ago, "[a]ll parties must be fully apprised of the evidence submitted or to be considered, and must be given opportunity to cross-examine witnesses, to inspect documents, and to offer evidence in explanation or rebuttal. ... for otherwise, even though it appeared that the order was without evidence, the manifest deficiency could always be explained on the theory that the Commission had before it extraneous, unknown, but presumptively sufficient information to support the finding." *ICC v. Louisville & Nashville Ry Co.*, 227 U.S. 88, 93 (1913).

The Tax Court's duty to disclose critical pieces of evidence and documents affecting the weight of such evidence is illustrated by this Court's decision in *Gonzales v. United States*, 348 U.S. 407 (1955). *Gonzales* held that a person seeking an exemption from military conscription as a conscientious objector was entitled to a copy of the Department of Justice's report to the Draft Appeals Board recommending that the exemption be denied. In rejecting the view that the Appeals Board could withhold the report, the Court noted that "our underlying concepts of procedural regularity and basic fair play" required that "a copy of the recommendation of the Department be furnished the registrant at the time it is forwarded to the Appeal Board, and that he be afforded an opportunity to reply." *Gonzales*, 348 U.S. at 412. The Court rejected the notion that the Appeals Board could withhold the report because it was "advisory," observing that precisely because the Appeals Board was "the only decision-making body to pass on the entire file," Gonzales needed to have the opportunity to reply to the Department of Justice's report in order to "insur[e] that this Board will have all of the relevant data." According to the *Gonzales* Court, "if the registrant is to present his case effectively to the Appeal Board, he must be cognizant of all the facts before the

Board as well as the over-all position of the Department of Justice." *Gonzales*, 348 U.S. at 413.

As with *Gonzales*, the relevant federal decision-maker in this case has been supplied with a report summarizing the results of an investigation and making factual recommendations. Just as Gonzales could not effectively present his case before the Appeals Board without knowing about the contents of the Department of Justice's report, so too, the Petitioners could not effectively present their case to the Tax Court without knowing the factual recommendations of the STJ. The trial before the STJ produced a voluminous record with over 5,000 pages of transcript, almost 5,000 pages of briefs, and thousands of exhibits. Faced with this undigested mass of evidence, the Petitioners could not be expected to focus its briefing and argument on the critical evidence — namely, those pieces of evidence that formed the basis of the STJ's report. The STJ's report would critically undermine certain legal theories and bolster others, by investing some witnesses' statements with a presumption of truth and other witnesses' statements with a presumption of falsity. Without knowing which witnesses were regarded by the STJ as credible, the Petitioners were incapable of showing to either the Tax Court itself in a post-trial motion or to the Seventh or Eleventh Circuits that the Tax Court committed clear error in light of the presumptively correct view of the facts. In effect, the Petitioners were denied the possibility of arguing that the Tax Court had failed to credit the presumptions that governed the evidence, because the Petitioners did not know how the STJ's report credited the evidence.

The Due Process clause forbids a tribunal from forcing the Petitioners to litigate in the dark, ignorant of the presumptions that govern the proof. Just as Gonzales "was entitled to know the thrust of the Department [of Justice]'s recommendation so he could muster his facts and arguments to meet its conten-

tions," *Gonzales* at 414, the Petitioners were entitled to know the recommendations of the STJ's report so that it could tailor its arguments before the Tax Court and the appellate courts to that report's presumptively correct view of the facts. There is no question but that *Gonzales* applies to the reports of hearings officers as well as advisory investigative reports. *See, e.g., Crotty v. Kelly*, 443 F.2d 214, 216-17 (1st Cir. 1971) (draft registrant seeking status as conscientious objector is entitled to copy of hearing officer's report, because otherwise registrant "could not effectively present his position to the Board"). Indeed, *Gonzales* applies with even greater force to the fact-findings of trial judges when those findings are invested with the legal status of being the presumptively correct view of the facts. The Selective Service Appeals Board in *Gonzales* was under no legal obligation to defer to the FBI report. By contrast, the Tax Court is legally obliged to defer to the STJ's findings on credibility.

C. Because the STJ's report is legally entitled to a presumption of being correct under Rule 183(c), that report is not part of the Tax Court's purely internal deliberations.

The Commissioner argues that the STJ's report was simply part of the internal process by which judges deliberate among themselves and, therefore, is immune from disclosure. Apparently drawing an analogy between draft judicial opinions and the STJ report, the Commissioner notes that "communications between the judges (and special trial judges) to whom a case is assigned for disposition are not produced or disclosed to the parties." Commissioner's Brief in Opposition to Cert., at 9.

This assertion, however, ignores the legal authority of the STJ's report. That report was not a purely internal communication between judges but rather the

officially sanctioned, legally required, and presumptively correct statement of findings by the trial judge. As the official statement of the judge's findings, it bore no resemblance to confidential judicial deliberations. Such internal deliberations have no legally operative effect on the parties or the tribunal itself. Therefore, disclosure of such documents to the parties would serve no purpose except to embarrass the tribunal with a judge's preliminary and perhaps tentative thoughts on a case. Thus, it is not surprising that courts universally hold that such deliberations should not be disclosed to the parties and that the tribunal's official opinion, not evidence of the judge's behind-the-scenes thought-processes, should determine the meaning and scope of the tribunal's decisions. *See, e.g., Fayerweather v. Ritch*, 195 U.S. 276, 306-07 (1904) (preclusive effect of trial judge's opinion determined by normal rules of *res judicata* rather than judge's later testimony of what he subjectively considered).

By contrast, under Rule 183(c), the STJ's report has at least some legal force and cannot be disregarded by the Tax Court at will: the Tax Court is legally bound to pay "due regard" to the report's evaluations of witnesses' credibility and generally accept the report's findings as presumptively correct. This report, therefore, is wholly unlike preliminary judicial discussions that have no legal effect on judicial discretion (*e.g.*, a draft of a judicial opinion, a law clerk's bench memo, or a staff attorney's recommendation), because the STJ's report constrains the Tax Court's discretion, if only in the sense that the Tax Court cannot ignore that report altogether. Disclosure of this legally constraining document is essential if the parties are to know the presumptions that govern the proof that they have submitted.

For the purpose of distinguishing the STJ's report from judges' internal deliberations, the precise level of deference owed by the Tax Court to the STJ's findings

is immaterial. Whether or not the Tax Court must uphold the STJ's findings absent clear error, as the D.C. Circuit has held, *Stone v. Commissioner*, 865 F.2d 342, 346-47 (D.C. Cir. 1989), it is indisputable that Rule 183(c) requires that "the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." Under the Tax Court's own rules, therefore, the STJ's report constrains the Tax Court's discretion to some degree. This rule follows the doctrine universally adopted by this and all lower courts that the findings of the officer who actually heard the testimony is, at the very least, highly relevant to the question of that testimony's credibility and thus to the question of whether an agency's decision is supported by substantial evidence. *Universal Camera*, 340 U.S. at 496; n.2 *supra*. Whatever the precise level of deference due to the STJ's report, it is beyond dispute that the Tax Court owes *some* deference to that report, if Rule 183(c) has any meaning whatsoever. Any such deference suffices to destroy any analogy between the report and purely internal judicial deliberations that can have no effect on the legal sufficiency of the evidence.

Rule 183(c)'s requirement of at least some minimal deference to STJ's report is not merely a technicality. Rather, it is the regulatory embodiment of an important due process requirement — namely, the requirement that the findings of the judge who actually hears the testimony will receive careful consideration by the ultimate decision-maker on the issue of the witnesses' credibility. Absent such careful consideration, the parties' oral presentation of evidence, their "day in court," becomes a meaningless exercise. Due process does not permit the ultimate decision-maker to dispense so cavalierly with consideration of the parties' own oral testimony, at least in the context of a traditional adjudication of a private individual's liberty or property interests. *Morgan v. United States*, 298 U.S. 468, 481 (1936)("If the one who determines the facts

which underlie the order has not considered evidence or argument, it is manifest that the hearing has not been given").[6]

The trial before the STJ was a traditional adjudication by an Article I judge of an individual's property rights. *Freytag v. Comm'r*, 501 U.S. 868, 881-82 (1991) (Special trial judges function as traditional judges in that they "take testimony, conduct trials, rule on the admissibility of evidence, and have the power to enforce compliance with discovery orders"). As with the hearing before any other trial judge, the hearing before the STJ was the parties' only opportunity to present in-person their version of events in a court of law. When a trial judge presides over the only venue in which the parties' in-person testimony can be heard, then the findings of that judge cannot be regarded as purely internal advice that the agency can withhold from the parties. *Cf. Willner v. Comm. on Character & Fitness*, 376 U.S. 96, 104 (1963) (rejecting the view that the Committee on Character & Fitness "is an investigator not a trier of facts" on the ground "the Appellate Division has held no hearings of its own to determine an applicant's character," indicating that "the role of the Committee is more than that of a mere investigator").

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[6] Whatever the force of *Morgan*'s famous statement that "[t]he one who decides must hear" in administrative decision-making, *Morgan*, 298 U.S. at 481, it has greater force in the context of adjudications an individual's property or liberty interests. *See United States v. Raddatz*, 447 U.S. 667, 681 n.7 (1980) ("we assume it is unlikely that a district judge would *reject* a magistrate's proposed findings on credibility when those findings are dispositive and substitute the judge's own appraisal; to do so without seeing and hearing the witness or witnesses whose credibility is in question could well give rise to serious questions which we do not reach").

D. Because the STJ's report is legally entitled to a presumption of being correct under Rule 183(c), that report is distinguishable from the reports of the Division of the Tax Court.

The legal status of the STJ's report also distinguishes it from the reports of the divisions of the Tax Court. Unlike the reports of the STJs, no rule of the Tax Court requires that the reports of the divisions of the Tax Court shall be presumed to be correct. Not surprisingly, 26 U.S.C. §7460 provides that this non-binding document "shall not be a part of the record in any case in which the chief judge directs that such report shall be reviewed by the Tax Court." Having no legally constraining effect on either the Tax Court or the parties, the Due Process clause does not require the disclosure of the division's reports. *Estate of Varian v. Comm'r of Internal Revenue*, 96 F.2d 753, 755 n.2 (9th Cir. 1968) (holding that report of division of Tax Court need not be disclosed). The non-disclosure of such non-binding decisions of the Division, however, do not suggest that the reports of the STJ can similarly be withheld. Unlike the division's reports, the STJ's reports are invested with the legal presumption of being correct. It is plausible that the Tax Court distinguished between the reports of the division and the STJ in this manner because, unlike the division judge who could append his or her findings to a dissenting opinion, the STJ has no mechanism for publishing its differing view of the evidence if the Tax Court were to reject the STJ's findings.[7] But regardless of the justification for the difference in the Tax Court's treatment of the reports of the division

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[7] As Judge Cudahy noted, "the STJs are not equal to the Tax Court judges and it might be naive to assume that the STJs have an equal voice in the collaborative process that results in Tax Court opinions." *Estate of Kanter*, 337 F.3d at 887 (Cudahy, J., dissenting).

and the STJ, the Tax Court does, in fact, treat the latter but not the former as presumptively correct. Having seen fit to confer such a legal status on the STJ's initial report, the Tax Court cannot then withhold such a critical document from the parties.

II. THE TAX COURT HAS NO LEGITIMATE REASON, SUCH AS AVOIDANCE OF ADMINISTRATIVE BURDEN, FOR REFUSING TO DISCLOSE THE STJ'S REPORT WHEN RULE 183(B) ALREADY REQUIRES THE STJ TO SUBMIT SUCH A REPORT TO THE TAX COURT.

Disclosure of the STJ's report would be virtually costless to the government. Indeed, the Commissioner has never described any burden that could result from such disclosure. The Petitioners do not ask the STJ to generate a new or different report, with the attendant delay and cost that such a task might entail. They ask only that the Tax Court simply disclose a report that already exists and is already required by the Tax Court's regulations. Rule 183(b) of the Tax Court's Rules of Practice and Procedure already require that "the Special Trial Judge shall submit a report, including findings of fact and opinion, to the Chief Judge [of the Tax Court]." Requiring that this already-existing report be disclosed imposes no significant "fiscal and administrative burdens" on the Tax Court. *Mathews v. Eldridge*, 424 U.S. at 348 (noting that "the Government's interest, and hence that of the public, in conserving scarce fiscal and administrative resources is a factor that must be weighed").

The Commissioner's brief in opposition to certiorari cites decisions holding that agencies are not always constitutionally required to create written fact-findings. *See* SG Brief in Opposition to cert., at 10 (citing *Utica Mut. Ins. v. Vincent*, 375 F.2d 129, 131 (2nd Cir. 1967)). But these cases are irrelevant to the

issue here. As this Court noted in *Gonzales v. United States*, 348 U.S. 407, 412 n.4 (1955), decisions addressing whether "a recommendation or intermediate report is necessary to begin with" are "inapplicable" to the distinct question of whether an agency must merely disclose a report that is already required by regulation or statute. It is, perhaps, arguable that, at least for certain sorts of "legislative" policy-making, an agency can reach a decision based on a paper record without even a written report of findings from the officer who actually heard the witnesses' testimony. *See Utica Mut. Ins. v. Vincent*, 375 F.2d 129 (2nd Cir. 1967).[8] But where a tribunal itself declares in its own rules that it will rely on a written report of a trial judge, then it defies common sense to say that the tribunal will somehow suffer some administrative burden if the report which the tribunal already possesses is disclosed to the parties.

Courts undoubtedly need some discretion to define for themselves how they will evaluate evidence. *Morgan v. United States*, 298 U.S. 468, 481 (1936) ("Assistants may prosecute inquiries. Evidence may be taken by an examiner. Evidence thus taken may be sifted and analyzed by competent subordinates. Argument may be oral or written. The requirements are not technical"). However, once the agency has exer-

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[8] As Judge Friendly emphasized in *Utica Mutual Insurance*, a hearing on whether a bargaining unit should be certified does not require trial-type procedures, because the nature of the underlying issue is more legislative than adjudicative, *Utica Mut. Ins.*, 375 F.2d at 132-33, and because "Utica has no 'property right' in the designation of the unit of its employees with which it may be required to bargain, even though the National Labor Relations Act entitles it to be heard thereon." *Id.* at 134. Where a tribunal adjudicates an individual's private rights, the failure of the tribunal to consider the report of the officer who actually heard the testimony raises more troubling issues of due process. *See, e.g., Cullen v. United States*, 194 F.3d 401, 406 (2nd Cir. 1999) (district judge may not reject magistrate's credibility judgments without having heard live witnesses, as this practice raises "troubling questions of constitutional due process.").

cised this discretion by giving a trial judge the power to make presumptively correct findings of fact, then that agency is estopped from saying that further disclosure of those findings is somehow unnecessary or impractical.

Indeed, the only apparent burden of disclosing the STJ's report is the burden of being forced to justify any discrepancies that might exist between the report of the STJ and Tax Court's opinion. But this is simply the normal burden of appellate review to insure that a decision is supported by sufficient evidence. Like any other court, the Tax Court has no legitimate interest in making such appellate review more difficult by making the evidentiary basis for its decision less transparent.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be reversed.

Respectfully submitted,

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IN THE

Supreme Court of the United States

ESTATE OF BURTON W. KANTER, *et al.*,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

BRIEF OF AMICI CURIAE PUBLIC CITIZEN, INC., and THE AMERICAN CIVIL LIBERTIES UNION IN SUPPORT OF PETITIONERS

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INTEREST OF AMICI CURIAE[1]

Public Citizen is a national nonprofit consumer advocacy organization with approximately 157,000 members. Its lawyers have extensive experience before regulatory agencies and the federal courts, and its work includes efforts to assure that the procedural rights of all persons are protected in the courts and agencies, including the right to see all relevant documents in a proceeding and the right to respond to all evidence and rulings. Public Citizen is filing this brief because the practices being challenged in this case threaten to undermine these procedural rights, and because it believes that its broad expertise can assist the Court in resolving the issues before it. Amicus takes no position on the merits of the underlying tax controversy.

The American Civil Liberties Union (ACLU) is a nationwide, nonprofit, nonpartisan organization with more than 400,000 members dedicated to the principles of liberty, equality, and fundamental fairness embodied in the Constitution and this nation's civil rights laws. Like Public Citizen, the ACLU believes those core principles are imperiled by the administrative practice challenged in this case. And, like Public Citizen, the ACLU takes no position on the underlying tax dispute between the parties.

INTRODUCTION AND SUMMARY OF ARGUMENT

The basic question presented by this case is whether Congress intended to authorize the Tax Court to create an adjudicative system in which the reports of Special Trial Judges, who conduct complex trials where credibility is a central issue, are kept secret and the parties have no opportunity to respond to those reports, either to the Tax Court Judge who decides the case or the Court of Appeals that reviews the

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[1] No person other than amici or their counsel authored this brief or made a monetary contribution toward its preparation. Letters of consent from the parties to the filing of this brief are on file with the Clerk.

decision. In cases where more than $50,000 is at stake, the Tax Court currently refuses to disclose fact-finding reports prepared by Special Trial Judges and submitted to Tax Court Judges, who alone are authorized to enter final decisions. As the summary of this system below makes clear, the relationship between Special Trial Judges and Tax Court Judges is nothing like that between two equal judges reaching a common result, or between a law clerk and a judge, or agency staff advising a decisionmaker, as the Government argued in its opposition to certiorari in this case.

The Tax Court's secretive treatment of Special Trial Judges' reports is an anomaly in the modern federal system. If these Special Trial Judge proceedings in the Tax Court were treated like similar two-level proceedings in either an Article III court or an administrative agency, the Tax Court would be required to disclose these reports and afford the parties an opportunity to comment. Nothing in the applicable statutes authorizes these secret procedures, and it cannot reasonably be concluded that Congress intended to permit the Tax Court to refuse to disclose the reports of Special Trial Judges when similar documents must be disclosed and used in further adversary proceedings in every other similar context in the federal system. [2]

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[2] In this case, the decision of the Tax Court was stated to be jointly that of the Tax Court Judge and the Special Trial Judge. That assertion has no bearing on the statutory question of whether the report prepared by the Special Trial Judge should have been disclosed to the parties and whether the parties should have been allowed to respond to the report and the factual findings contained therein, both in the Tax Court and in the Court of Appeals.

ARGUMENT

CONGRESS DID NOT INTEND TO AUTHORIZE THE TAX COURT TO REFUSE TO DISCLOSE THE REPORTS OF SPECIAL TRIAL JUDGES AND DENY PARTIES AN OPPORTUNITY TO RESPOND TO THEM.

I. The Role of Special Trial Judges in the Tax Court System.

In 1986, Congress authorized the Tax Court to appoint Special Trial Judges (STJs) to assist the Tax Court in its duties. *See* 26 U.S.C. § 7443A(a). *See generally Freytag v. Comm'r of Internal Revenue*, 501 U.S. 868 (1991). Special Trial Judges are appointed by the Chief Judge of the Tax Court and are paid 90% of the salary of a Tax Court Judge. *Id.* at (a) & (d). Congress specified four defined categories of cases on which STJs could sit, plus any others to which they were assigned by the Chief Judge. *Id.* at (b). Congress also authorized STJs to render final decisions, subject to further review as specified by the Tax Court, only in those four categories of cases. *Id.* at (c). Notably, Category (3) in subsection (b) consists of cases in which the amount of the tax dispute does not exceed $50,000. In such larger cases, therefore, the final decision may be made only by a Tax Court Judge. Although Congress did not spell out the relationship between the STJ and the Tax Court Judge, that issue is addressed in Tax Court Rule 183.

Where an STJ is designated to serve as an initial fact-finder, he submits a report, including findings of fact and an opinion, to the Chief Judge of the Tax Court. Tax Ct. R. 183(b). The Chief Judge then assigns the case to a Tax Court Judge (or a division, which is composed of one or more Tax Court judges, 26 U.S.C. § 7444(c)), who "may adopt the Special Trial Judge's report or may modify it or may reject it in whole or in part, or may direct the filing of additional briefs or may receive further evidence or may direct oral ar-

gument, or may recommit the report with instructions." Tax Ct. R. 183(c). That Rule also instructs Tax Court Judges that, in performing their functions, they must give "[d]ue regard ... to the circumstance that the Special Trial Judge had the opportunity to evaluate the credibility of witnesses, and the findings of fact recommended by the Special Trial Judge shall be presumed to be correct." None of these provisions of Rule 183 is objectionable. What is challenged is the practice, not contained in any Rule or statute, under which the Court refuses to disclose STJ reports, let alone allow the parties to respond to the findings contained in them, regardless of whether the Tax Court Judge adopts or rejects the STJ's findings.

One additional part of this system bears on that challenge, the statute that authorizes judicial review of Tax Court decisions, 26 U.S.C. § 7482. Subsection (a)(1) requires that Tax Court decisions be judicially reviewed "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury." That review is governed by Rule 52(a) of the Federal Rules of Civil Procedure, which requires the trial judge to make factual findings (as does Tax Court Rule 183) and only allows them to be set aside, "whether based on oral or documentary evidence," if they are "clearly erroneous [with] due regard ... given to the opportunity of the trial court to judge the credibility of the witnesses." However, under the current Tax Court practice, the report containing STJ's findings of fact—a document that Judge Cudahy called the single most significant item in evaluating a Tax Court decision on fraud in cases like this—*Kanter v. Comm'r of Internal Revenue*, 337 F.3d 833, 886 (7th Cir. 2003) (Cudahy, J., dissenting)—is never shown to the parties or the appeals court. Thus, the reviewing court in STJ cases has no realistic means to carry out the requirement, imported from Rule 52(a), that "due regard" shall be given to the trial judge's assessment of the witnesses because it has no idea whether the Tax Court Judge agreed or disagreed with

the credibility findings of the STJ, who was the one who conducted the trial.

The principal question in this case is whether this secretive practice is contrary to the intent of Congress in establishing the system by which Special Trial Judges are used by the Tax Court in cases involving disputes of more than $50,000. Whatever may be said in defense of this practice, there is no basis, as the Government has urged, to analogize it to the relation between a law clerk and a judge, or between two coequal judges working on a draft of an opinion. Moreover, as we now show, this system is so contrary to every other similar federal system that it cannot have been what Congress intended. Indeed, as the petitioners' briefs argue, this system raises serious due process concerns, which present another reason not to assume that Congress intended to permit the STJ reports to be withheld by the Tax Court.

II. The Tax Court's Refusal to Disclose the Fact-Finding Reports of STJs and Afford Parties an Opportunity to Comment on Them Is an Anomaly in Modern Federal Law.

The Tax Court's secretive treatment of STJ fact-finding reports is aberrant. In every other federal judicial proceeding where an initial fact-finder conducts the trial and submits a report for consideration by a judge empowered to enter a final decision, the initial fact-finder's report is included in the record and served on the parties, who are then given an opportunity to respond. Nothing in the applicable statutes signals that Congress intended to authorize the Tax Court to deviate from this universal practice of disclosing initial fact-finders' reports to parties and reviewing courts.

The role of STJs in the Tax Court is very similar to that of magistrate judges in the district courts. Congress has granted magistrates the authority to decide certain classes of civil cases and to make recommendations to decisionmakers in others. 28 U.S.C. § 636(b)(1). In those cases where only

limited authority is granted, magistrates serve an initial fact-finding function in the district courts, similar to that performed by STJs in the Tax Court in cases involving more than $50,000. Yet Congress has mandated that fact-finding reports written by magistrate judges in the district courts—reports very similar to those written by STJs in the Tax Court—be included in the record and served on the parties. 28 U.S.C. § 636(b)(1)(C). Parties then have the right to file written objections to the proposed findings before the district court judge makes his final decision. *Id.* [3]

There is no obvious policy rationale for the Tax Court to diverge from the procedural transparency of the district courts in their disclosure of magistrates' reports. In fact, the Tax Court has less authority in reviewing fact-finding reports than do the district courts. The Tax Court is required to presume that factual findings are correct under Rule 183, whereas in some situations the district court must perform de novo review of rulings by magistrates. 28 U.S.C. § 636(b)(1)(C). Without disclosure of STJ reports, there is no way of knowing whether the Tax Court Judge afforded the STJ's findings the proper level of deference.

Disclosure of magistrates' reports also enables reviewing courts to determine whether a district court properly accepted or rejected a magistrate's proposed findings on credibility. In *United States v. Raddatz*, 447 U.S. 667 (1980), where a magistrate conducted a suppression hearing and made credibility judgments, this Court suggested that due process may be violated if a district judge rejects a magistrate's proposed findings without having heard or seen the witnesses. In criminal

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[3] Even before the enactment of the current section 636 in 1976, the failure of a district court to give parties an opportunity to be heard before adopting a magistrate's recommendation to grant a preliminary injunction was considered to be "an abnegation of judicial authority by the court entirely contrary to the provisions of Article III." *Reed v. Board of Election Comm'rs*, 459 F.2d 121, 123 (1st Cir. 1972).

cases, several courts have since held that, where a magistrate finds in favor of a defendant on a disputed issue of fact, the district court cannot reject that finding and rule in favor of the Government without providing a new hearing at which the judge can determine firsthand the credibility of the witnesses. To do otherwise may violate due process and Article III. *See, e.g., Cullen v. United States*, 194 F.3d 401, 406 (2d Cir. 1999) (district judge may not reject magistrate's credibility judgments without having heard live witnesses, as this practice raises "troubling questions of constitutional due process") (citation omitted); *United States v. Mejia*, 69 F.3d 309 (9th Cir. 1995); *Hill v. Beyer*, 62 F.3d 474 (3d Cir. 1995); *Proffitt v. Wainwright*, 685 F.2d 1227 (11th Cir. 1982); *Louis v. Blackburn*, 630 F.2d 1105, 1106 (5th Cir. 1980) (due process requires that district judge either accept magistrate's credibility determinations or make independent decision after hearing live testimony). Similar reasoning applies to STJ reports in the Tax Court because it is the STJ, not the Tax Court judge, who has seen and heard the witnesses.

Similarly, Special Masters, appointed by Article III courts to recommend findings of fact to a judge authorized to make a final decision, Fed. R. Civ. P. 53(a)(1)(B), play a role comparable to that of STJs. Fact-finding reports of Special Masters must be served on each party and filed with the court. Fed. R. Civ. P. 53(f). Before acting on Special Masters' reports, courts must also accord the parties an opportunity to be heard. Fed. R. Civ. P. 53(g). *See Kieffer v. Sears, Roebuck & Co.*, 873 F.2d 954 (6th Cir. 1989) (remanding for further proceedings when a Special Master's report and recommendation was adopted by the district court without giving the appellant an opportunity to be heard).

In the field of bankruptcy, in non-core proceedings, bankruptcy judges submit proposed findings of fact and conclu-

sions of law to the district court, to which parties are entitled to file objections. 28 U.S.C. § 157(c)(1). [4] The role of bankruptcy judges in conducting trials of non-core cases and submitting recommendations to final decisionmakers is analogous to that of STJs in cases over $50,000. Like STJs, who are inferior officers of the United States (*Freytag*, 501 U.S. at 881-83), bankruptcy judges cannot constitutionally decide certain claims on their own. *See Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982). However, in the bankruptcy court, unlike the Tax Court, the fact-finding reports of bankruptcy judges must be disclosed, and parties must be given an opportunity to respond to them before the district court enters a final decision. Fed. R. Bankr. P. 9033.

This Court in *Freytag* narrowly concluded that the Tax Court was a court of law, not a "department" under the Appointments Clause. 501 U.S. at 890. Nonetheless, as an Article I court, the Tax Court has many attributes of an administrative agency, and hence analogizing its operation to the administrative context is instructive. The reports of administrative law judges ("ALJs") in federal administrative law cases tried under the formal adjudication provisions of the Administrative Procedure Act, 5 U.S.C. § 554, 556 & 557, must be disclosed. The APA provides that all "initial, recommended and tentative decisions" in such cases are made part of the record, including the findings of an ALJ, which are analogous to those of an STJ in the Tax Court. 5 U.S.C. § 557(c). The APA also gives parties the right to respond to an ALJ's report by submitting proposed findings, exceptions to recommended decisions, or supporting reasons for, and

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[4] Section 157(c)(1) is drawn from 28 U.S.C. § 636(b)(1) (part of the United States Magistrate Act). These statutes contain analogous provisions for proposed findings and recommendations to be made by initial fact-finders and submitted to district judges. 1-3 COLLIER ON BANKRUPTCY ¶ 3.303 [2] (15th ed.).

exceptions to, proposed findings. 5 U.S.C. § 557(c). The purposes of Section 557(c) "are to preserve objections in the record and to inform the parties and any reviewing body of the disposition of the case and the grounds upon which the agency's 'decision' is based." *Borek Motor Sales, Inc. v. NLRB*, 425 F.2d 677, 681 (7th Cir. 1970).

In *Universal Camera v. NLRB*, 340 U.S. 474 (1951), this Court held that effective Article III review of an agency decision necessitated consideration of the ALJ's fact-finding report and whether any departures from the report by the agency were justified. "Evidence supporting a conclusion may be less substantial when an impartial, experienced examiner who has observed the witnesses and lived with the case has drawn conclusions different from the Board's." *Id.* at 496. *See also Edwards v. Sullivan*, 985 F.2d 334, 338 (7th Cir. 1993) (holding that a reviewing court will not reassess credibility determinations made by an ALJ as long as they find some support in the record). As this Court noted, "[s]urely an examiner's report is as much a part of the record as the complaint or the testimony." *Universal Camera,* 340 U.S. at 493.

Other courts have held that "intelligent appellate review" requires that the reviewing court be informed of both the basis for an ALJ's decision and the agency's treatment of that decision. *See, e.g., Armstrong v. Commodities Futures Trading Comm'n*, 12 F.3d 401, 403-04 (3d Cir. 1993) (when court could not tell from Commission's opinion which parts of the ALJ's decision it adopted and which parts it rejected, "the Commission's conclusion that the ALJ reached a 'substantially correct' result leaves questions about which specific findings or conclusions by the ALJ were incorrect").

The courts of appeals agree that, when an agency rejects the findings of an ALJ, it must explain its reasoning carefully and plausibly. "The Board's departure from the ALJ's findings is vulnerable if it fails to reflect attentive consideration to the ALJ's decision." *Citizens State Bank of Marshfield v.*

FDIC, 718 F.2d 1440, 1444 (8th Cir. 1983). *See also, e.g., In re United Corp.*, 249 F.2d 168, 178-79 (3d Cir. 1957); *Greater Boston Television Corp. v. FCC*, 444 F.2d 841, 853 (D.C. Cir. 1970); *American Federation of Television and Radio Artists v. NLRB*, 395 F.2d 622, 628 (D.C. Cir. 1968) ("Because the Board reversed the Examiner without hearing oral argument, we have given particular attention to the question whether the Board's findings are vulnerable for failure to reflect attentive consideration of the Examiner's decision."); *Retail Store Employees Union v. NLRB*, 360 F.2d 494, 495 (D.C. Cir. 1965) (holding NLRB's departure from an ALJ's decision invalid where the Board simply expressed the belief that facts relied upon by the examiner did not support the examiner's finding). Obviously, if a reviewing court is not given access to ALJ reports, or in this case STJ reports, it cannot determine whether the agency (Tax Court) gave sufficient consideration to the findings of the person who actually saw and heard the witnesses.

State courts have also adopted the practice of disclosing initial fact-finding reports. In *Mazza v. Cavicchia*, 105 A.2d 545, 557 (N.J. 1954), the New Jersey Supreme Court, in an opinion by Chief Justice Arthur Vanderbilt, held that failure to disclose an ALJ's report violated due process:

> [W]e have not been able to find a single case in any state of the Union, nor have any been cited to us, justifying or attempting to justify the use of secret reports by a hearer to the head of an administrative agency. To approve such a practice in deciding an administrative controversy would be to confer on New Jersey the dubious distinction of being the only jurisdiction in the United States to ignore a fundamental element of due process and fair play.

State courts have continued to follow the *Mazza* approach. *See* BERNARD SCHWARTZ, ADMINISTRATIVE LAW 437 n.13 & n.14 (3d ed. 1991).

Indeed, prior to 1983, the Tax Court also followed this model of disclosing reports of initial fact-finders. In 1943, Congress authorized the Tax Court to appoint commissioners, the precursors to STJs, to hold hearings and make initial determinations in tax disputes. HAROLD DUBROFF, THE UNITED STATES TAX COURT: AN HISTORICAL ANALYSIS 346 (1979). The Tax Court promulgated Tax Court Rule 48, requiring commissioners to conduct hearings and giving the parties 30 days to propose findings of fact before the commissioner submitted a report of his/her findings to the court. The report was then served on the parties, who had a right to file exceptions. *Id.* At that time, Tax Court Rule 182(b) specifically mandated that commissioners' reports be disclosed. *See* 60 T.C. 1149 (1973).

The title "commissioner" was changed to "special trial judge" by the Tax Reform Act of 1984, § 464(a), 98 Stat. 824. Then, in section 1556(a) of the Tax Reform Act of 1986, 100 Stat. 2754, Congress gave STJs the authority to hear and decide certain classes of cases as described in 26 U.S.C. §§ 7443A(a) and (b). Meanwhile, in 1983, the Tax Court had repealed the disclosure requirement so that STJ reports were no longer required to be disclosed to the public and hence were no longer routinely available to the parties and the courts of appeals. *See* 81 T.C. 1069 (1983) (amending Rule 182 and renumbering it to Rule 183). The Tax Court provided no contemporaneous explanation of any problems encountered under its prior system of disclosing initial fact-finders' reports, nor any reason why it needed to be changed.

In contrast with this lack of authority to keep STJ reports secret, Congress has actually provided for a procedure very close to what the Tax Court did in this case, but in a different context. Under 26 U.S.C. § 7458, both the taxpayer and the Secretary have an absolute right to be heard before a division of the Tax Court, but if the case is subsequently considered by the full Tax Court, pursuant to section 7460(b), "neither the taxpayer nor the Secretary shall be entitled to notice and

an opportunity to be heard before the full Tax Court upon review." Although the statutes do not specify that the report of the division in that situation is not made public when it is issued, that is our understanding of the practice. That is also consistent with, if not commanded by, the final sentence of section 7460(b), which provides that the report of the division "shall not be part of the record" in cases reviewed by the full Tax Court because in that situation the full Tax Court is making a de novo determination on the question presented. As the briefs of petitioners demonstrate, en banc consideration by the Tax Court is utilized for questions of law, in contrast to the fact questions at issue in this case and in others tried before STJs. Accordingly, this explicit congressional creation of the very type of system followed here, but in a different context, further underscores the impropriety of its use of secret STJ reports in cases required to be decided by a Tax Court Judge. The lack of explicit congressional authority for the Tax Court to use its current STJ system is particularly significant in light of the fact that the system governing review by the full Tax Court was in place for many years before the office of STJ was created in 1986.

In every other American judicial proceeding where an initial fact-finder submits a report for consideration by a judge empowered to make a final decision, the initial fact-finder's report must be included in the record. If the Tax Court were considered either an Article III court or an administrative agency subject to the APA, it would be compelled to disclose the STJ's reports and accord parties an opportunity to comment on the report before any final decision was made. Yet the Tax Court, which decides cases with substantial amounts at stake, refuses to disclose the fact-finding reports of STJs. This Tax Court practice is so unique that, without specific statutory authorization, it is unreasonable to conclude that Congress intended to deviate from the universal practices in comparable court and agency contexts when

it authorized STJs to conduct complex trials involving substantial tax liabilities.

III. The Tax Court's Refusal to Include Rule 183 Reports in the Record Undermines the Fundamental and Universal Adjudicative Practices for Assuring Fair and Effective Judicial Review.

The Tax Court's current treatment of Rule 183 reports as secret documents impedes meaningful adversarial comment and judicial review—practices that Congress has legislated to protect in analogous areas of law. In refusing to include STJ reports in the record, the Tax Court departs from the fundamental American legal doctrine that all evidence on which a decision rests must be included in the trial record, and that record must constitute the exclusive basis for decision. *E.g.*, *West Ohio Gas Co. v. Public Utilities Comm'n of Ohio*, 294 U.S. 63, 69 (1935). Furthermore, in refusing to disclose STJ findings to the parties, the Tax Court departs from the established adjudicative principle that notice and an opportunity to be heard is a basic requirement of a fair hearing. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 313 (1950). As a result, parties in the Tax Court are denied the opportunity to comment on preliminary findings contained in the STJ report. More importantly, if the Tax Court Judge disagrees with the factual findings of the STJ, the parties and the appeals court will never learn of this disagreement, despite the requirement that the reviewing court give deference to the findings of the judge who heard and saw the witnesses. 26 U.S.C. § 7482(a)(1).

The need for disclosure of all evidence to ensure a complete record for review and opportunities for adversarial comment has led Congress and the judiciary to restrict ex parte communications and improper judicial notice. Congress has banned ex parte communications "relevant to the merits of the proceeding" between any "interested person" and agency decisionmakers in hearings required to be on the record. 5 U.S.C. § 557(d). *See, e.g.*, *PATCO v. Federal Labor*

Relations Authority, 685 F.2d 547, 562 (D.C. Cir. 1982) (broadly construing term interested person to further goals of ex parte prohibition); *Portland Audubon Soc. v. Endangered Species Comm.*, 984 F.2d 1543 (9th Cir. 1993) (holding that off the record communications between White House officials and decisionmakers in a formal hearing violated Section 557 of the APA). Congress has also mandated that, when prohibited ex parte communications do occur, the decisionmaker must include the communications in the public record. 5 U.S.C. § 557(d)(1)(C). Judicial notice has also been restricted. All facts that can be reasonably disputed must be proven at trial. *See* Fed. R. Evid. 201 (limiting judicially noticed facts to those "not subject to reasonable dispute"). In *Ohio Bell Telephone Co. v. Public Utilities Comm'n,* 301 U.S. 292, 303 (1937), a company's right to a fair and open hearing under the Fourteenth Amendment was violated when the agency failed to disclose the facts of which it took official notice and on which it based its decision. As this Court noted, judicial review could become meaningless if broad judicial notice were authorized as a regular practice. *See also, e.g., West Ohio Gas Co.*, 294 U.S. at 77.

Even in cases not required to be heard and decided on the record, the judiciary has recognized the importance of full disclosure to assure meaningful judicial review. *See Citizens to Preserve Overton Park, Inc. v. Volpe*, 401 U.S. 415, 416 (1971) (reviewing court must have access to the basis of the agency's decision in order to conduct a "searching and careful" inquiry to determine whether the ruling was based on consideration of relevant factors). In cases where there is no requirement for an on the record hearing, such as informal adjudications and rulemakings governed by the notice and comment procedures of 5 U.S.C. § 553, ex parte communications that are not included in the public record have been held inconsistent with APA requirements for judicial review. *E.g., United States Lines, Inc. v. Federal Maritime Comm'n*, 584 F.2d 519, 540-41 (D.C. Cir. 1978) (Commission's reliance

on ex parte communications not recorded in the public record deprived the public of a meaningful opportunity to participate and effectively foreclosed judicial review, even where proceeding was not required to be on the record). In *Home Box Office, Inc. v. Federal Communications Comm'n*, 567 F.2d 9, 54 (D.C. Cir. 1977), the court noted that the agency's secrecy and failure to include all of the bases for its decision in the record impeded the reviewing courts in their evaluation of the agency's actions for arbitrariness or inconsistency with delegated authority. "Even the possibility that there is here one administrative record for the public and this court and another for the Commission and those 'in the know' is intolerable." *Id.* at 54. *See also Sangamon Valley Television Corp. v. United States*, 269 F.2d 221 (D.C. Cir. 1959) (remanding a licensing case to the FCC for an evidentiary hearing to bring to light all information presented to FCC members off the record and give parties a chance to comment); *United States Lines*, 584 F.2d at 535 (holding that an agency must disclose and specify all evidence relied on by the decisionmaker in sufficient detail to allow for meaningful adversarial comment); *Home Box Office, Inc., supra* (remanding so that the extent and content of ex parte communications could be added to the record and parties could be accorded a chance to comment).

Congress and the judiciary also require that parties be given an opportunity to explain, rebut, or support evidence obtained through official or judicial notice: "[w]hen an agency decision rests on official notice of a material fact not appearing in the evidence in the record, a party is entitled, on timely request, to an opportunity to show the contrary." 5 U.S.C. § 556(e); Fed R. Evid. 201(e) (affording right to be heard on propriety of judicial notice). Adversarial comment is so basic to fair and open adjudication in our legal system that the full hearing required by due process cannot be provided without it. *See, e.g., Morgan v. United States*, 304 U.S. 1, 18 (1938); *Ohio Bell Telephone Co.*, 301 U.S. at 292; *West*

Ohio Gas Co., 294 U.S. 63 (holding that due process was denied when a party was not given an opportunity to supplement or explain evidence taken on judicial notice).

Adversarial comment is also needed to illuminate assertions of fact and expert opinion that may be biased, inaccurate, or incomplete. *See Home Box Office*, 567 F.2d at 55; *United States Lines*, 584 F.2d at 534.

> An unjust decision may very likely be the result where no opportunity is given to those affected to call attention to such mistakes. That is why it is a fundamental principle of all adjudication, judicial and administrative alike, that the mind of the decider should not be swayed by materials which are not communicated to both parties and which they are not given an opportunity to controvert.

Mazza, 105 A.2d at 555. Furthermore, providing opportunities for adversarial comment can ensure that all questions will be raised and all evidence will be submitted by the parties prior to judicial review. Conversely, if opportunities for adversarial comment are lacking, factual questions underlying a ruling may be raised for the first time on judicial review. *See United States Lines*, 584 F.2d at 534 ("[O]ur insistence that this information be revealed during the agency proceedings not only serves the interests of the parties and the court, but also preserves the prerogatives of the agency to address in the first instance the questions of law and fact raised by its action.").

Although somewhat different from situations involving ex parte communications or expansive official notice, the failure to make public the STJ report also frustrates the ability of a reviewing court to perform its assigned duties and impedes the adversarial process. In this and other STJ cases, the evidentiary record is complete and was fully available to all parties, and in that sense, the ex parte and official notice problems do not exist. Non-public evidence, as such, is not the problem. Rather, the problem is that the record lacks the

evaluation by the STJ of important issues of fact—especially issues of credibility which can be critical in cases of fraud such as this—that are part of the undisclosed report of the STJ who tried the case. As the discussion above demonstrates, the views of the initial fact-finder who heard and saw the witnesses are vital in a court's assessment of whether the factual findings made by the agency or the lower court can be sustained.

The Tax Court's refusal to include Rule 183 reports in the record is inconsistent with Congress's policy of ensuring effective judicial review and adversarial comment. The Tax Court has never given any reason why it should be permitted to continue a practice which so clearly undermines judicial review and the adversarial process, and which is not permitted in comparable cases elsewhere in the federal system. Accordingly, this Court should construe the applicable statutes not to confer on the Tax Court the right to require that STJ reports be kept secret from the parties and the courts of appeals and the right to deny all parties the opportunity to respond to the STJ's proposed findings.

* * *

Amici do not understand why the Government is defending the Tax Court's system, beyond the fact that the IRS won this particular case in the Tax Court. The process by which decisions are reached in cases tried before STJs, however, could also result in losses for the IRS in the Tax Court, which would be much more difficult for it to overturn on appeal. Perhaps the explanation for the Government's defense of these procedures is that the IRS is a repeat player and that, by and large, the current system benefits it more than the traditional one that petitioners and this amicus brief support. Whatever the reason, it is unfortunate that the Government did not look at the issue differently, more in line with the etching on the Justice Department's headquarters: "The Government wins when justice is done." *Cf. Berger v. United States,* 295 U.S. 78, 88 (1935) (the interest of the United

States in a criminal case "is not that it shall win a case, but that justice shall be done").

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be reversed, and the case remanded to the Tax Court with instructions that the report of the Special Trial Judge should be served on the parties and a reasonable opportunity be provided to them to submit objections or supporting statements concerning that report to the Tax Court Judge to whom the case is assigned.

Respectfully submitted,

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